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No. 856

No. 15399

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# United States Court of Appeals

## for the Ninth Circuit

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EDWARD POOL and LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY and EDNA MURPHY,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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# Transcript of Record

In Two Volumes

VOLUME I.

(Pages 1 to 258, inclusive)

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Petitions to Review Decisions of the Tax Court of the United States

FILED
FEB 27 1957
PAUL P. O'BRIEN, CLERK

# No. 15399

# United States
# Court of Appeals
## for the Ninth Circuit

EDWARD POOL and LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY and EDNA MURPHY,

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]


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## NAMES AND ADDRESSES OF ATTORNEYS

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Assistant United States Attorney,

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Washington 25, D. C.,

Attorneys for Respondent.

The Tax Court of the United States

Docket No. 36108

EDWARD POOL and LOTTIE POOL,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Appearances:
For Petitioner: Arthur Groman, Esq., Irving I. Axelrad, Esq.
For Respondent: Charles Chase, Esq., Donald P. Chehock, Esq.

## DOCKET ENTRIES

1951

Aug. 8—Petition received and filed. Taxpayer notified. Fee paid.

Aug. 8—Copy of petition served on General Counsel.

Aug. 8—Request for Circuit hearing in Los Angeles filed by taxpayer. 8/21/51 granted.

Oct. 4—Answer filed by General Counsel.

Oct. 11—Copy of answer served on taxpayer. Los Angeles.

1952

Oct. 7—Hearing set Dec. 1, 1952, Los Angeles.

Dec. 3—Hearing had before Judge Raum on petitioner's motion to continue, granted, continued generally, appearance of Irving I. Axelrad filed at hearing.

1953

Jan. 8—Hearing set Feb. 24, 1953, Los Angeles.

Feb. 27, Mar. 2, 3, 4—Hearing before Judge Turner on merits, stipulation of facts with exhibits 1-3 thru 18-R, filed. Briefs 6/4/53. Replies 9/17/53.

Mar. 24—Transcript of hearing 2/27/53 filed.

Mar. 24—Transcript of hearing 3/2/53 filed.

Mar. 24—Transcript of hearing 3/3/53 filed.

Mar. 24—Transcript of hearing 3/4/53 filed.

May 29—Joint motion for extension to 8/31/53, to file briefs filed. 6/2/53 granted.

Aug. 31—Brief filed by taxpayer. 9/3/53 copy served.

Sept. 1—Motion for leave to file the attached brief, brief lodged, filed by General Counsel. 9/1/53 granted. 9/3/53 Served.

Oct. 15—Reply brief filed by taxpayer. 10/16/53 copy served.

1956

Mar. 20—Memorandum findings of fact and opinion filed, Turner, J. Decision will be entered under Rule 50. 3/21/56 copy served.

July 31—Agreed computation for entry of decision, filed.

Aug. 20—Decision entered, Judge Turner, Division 8. Served 8/21/56.

Nov. 5—Petition for review by United States Court of Appeals, Ninth Circuit, with statement of service attached, filed by petitioner.

1956

Nov. 9—Proof of service filed.

Nov. 14—Designation of contents of record on review with proof of service thereon, filed.

Dec. 4—Order extending time for filing record on review and docketing petition for review to Feb. 3, 1957, entered.

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[Title of Tax Court and Cause.]

## PETITION

The above named petitioners hereby petition for a redetermination of the deficiencies set forth by the Commissioner of Internal Revenue in his notice of deficiency (Bureau Symbols LA:IT:90D:LHP) dated May 17, 1951, and as a basis for their proceeding, allege as follows:

1. Petitioners are, and at all times mentioned herein were, husband and wife, with residence at 735 Bonhill Road, Brentwood, California. The return for the period herein involved was filed with the Collector for the Sixth District of California.

2. The notice of deficiency (a copy of which is attached hereto and marked Exhibit "A") was mailed to the petitioners on May 17, 1951.

3. The deficiency as determined by the Commissioner, is in income taxes for the calendar year 1948, in the amount of $29,399.88. The entire amount of the deficiency is in dispute.

4. The determination of tax set forth in the

said notice of deficiency is based upon the following errors:

(a) In determining income tax for the year 1948, the Commissioner erroneously increased the petitioners' taxable income by the amount of $107,908.23 by treating the said sum as ordinary income instead of accepting the long term capital gain pertaining thereto reported by the petitioners.

5. The facts upon which the petitioners rely as the basis for their proceeding are as follows:

(a) Beginning in 1943, the petitioners and other individuals (William K. Murphy and Edna Murphy) entered into a contract with Arteraft Builders, Inc., to build for them certain rental housing consisting of small duplexes. Upon completion, pursuant to a prior written agreement, the duplexes were transferred to the four individuals, including the petitioners, each of whom took an undivided one-fourth interest. The four individuals originally caused the duplexes to be built and acquired solely for the purpose of operating the duplexes as a source of rental income. From the outset of the acquisition of the land and construction of the buildings it was the firm intent and purpose of the petitioners and the other said individuals to operate the duplexes as rental property, and it was not their purpose to sell them. Pursuant to their plan, petitioners and the others rented the duplexes to individual tenants under leases running from one to three years.

(b) The petitioners and the other said persons, at all times herein mentioned, were not engaged in

the business of buying or selling real estate, did not buy or sell any real estate, nor did any of them possess real estate brokers' licenses, nor had any of them ever owned a real estate broker's license, nor had they at any time been engaged in the business of buying or selling real estate.

(c) From the date of the acquisition of the said duplexes, the petitioners and the other said persons filed a return on the rentals from the properties through a return labeled "Edward Pool & Associates." This was not a formal partnership, but a means of complying with the law requiring filing of a return of a joint enterprise.

(d) The said duplexes were constructed pursuant to the provisions of Title 6 of the Defense Housing Act, solely for rental purposes and they continued to be operated solely for rental purposes. By the year 1946, however, the real estate values of the duplexes had so increased that the rentals received by the petitioners and the others did not represent a fair return on the then value of the duplexes. Accordingly, petitioners and the others determined to sell the duplexes and to put their capital into other investments. Petitioners and the other said persons turned the selling of the duplexes over to a licensed real estate broker and took no part personally in the sale.

(e) Inasmuch as the petitioners were not engaged in the business of buying and selling real estate, petitioners, in their 1948 return,, reported the difference between the base of the duplexes sold in that year and the sales price realized as a long

term capital gain, more than six months having elapsed in every instance between the petitioners' acquisition of their interest in the duplexes and the disposition thereof.

Wherefore, petitioners pray that this Court may hear the proceeding and determine that there is no deficiency in income taxes against the petitioners for the calendar year 1948.

/s/ ARTHUR GROMAN
Counsel for Petitioner

Of Counsel:
Mitchell, Silberberg & Knupp

Duly Verified.

EXHIBIT "A"

Form 1279 (Rev. July 1948)

Treasury Department, Internal Revenue Service,
417 South Hill Street, Los Angeles 13, Calif.

Office of Internal Revenue Agent in Charge, Los Angeles Division. LA:IT:90D:LHP

Mr. Edward Pool, and Mrs. Lottie Pool,
Husband and Wife May 17, 1951
3465 West 54th Street, Los Angeles 43, California

Dear Mr. and Mrs. Pool:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1948 discloses a deficiency of $29,399.88, as shown in the statement attached.

In accordance with the provisions of existing in-

ternal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Los Angeles, California, for the attention of LA:CONF. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

Geo. J. Schoeneman,
Commissioner,
/s/ By George D. Martin,
Internal Revenue Agent in Charge

LHP:vmc—Enclosures: Statement, Form of waiver

STATEMENT

Tax Liability for the Taxable Year Ended December 31, 1948

Income tax—Deficiency: $29,399.88.

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated October 23, 1950, to your protest dated December 8, 1950, and to the statements made at the conferences held.

A copy of this letter and statement has been mailed to your representative, Mr. Erwin Lampe, 612 South Flower Street, Los Angeles 17, California, in accordance with the authorization contained in the power of attorney executed by you.

## Adjustments to Net Income

| | |
|---|---|
| Net income as disclosed by return | $ 34,361.11 |
| Additional income: | |
| (a) Income from partnership increased | 107,908.23 |
| Total | $142,269.34 |
| Reduction of income: | |
| (b) Net capital gain from partnership | 53,954.11 |
| Net income adjusted | $ 88,315.23 |

## Explanation of Adjustments

(a) Your respective shares of the distributive income of the partnership, Edward Pool and Associates, for its fiscal year ended January 31, 1948, has been increased as follows:

| | |
|---|---|
| Your shares of the distributive income per the partnership return for the fiscal year ended January 31, 1948 | $ 5,693.06 |
| Increase | 107,908.23 |
| Total as adjusted | $113,601.29 |

In determining the partnership income distributable to you as above, the following adjustments have

been made for the partnership's fiscal year ended January 31, 1948:

| | | |
|---|---|---|
| Net income per partnership return | | $ 11,386.12 |
| Add: Ordinary income on sale of real property reported as capital gain by the individual partners | | 217,354.06 |
| | | $228,740.18 |
| Deduct: Deduction allowable for equipment abandoned | | 1,537.60 |
| Adjusted net income of partnership | | $227,202.58 |
| Total of your distributable shares | | $113,601.29 |

(b) Pursuant to the foregoing adjustment, the amount of $53,954.11 included in the income reported in your return as your share of net capital gain realized by the above-named partnership is eliminated therefrom.

## Computation of Tax

| | | |
|---|---|---|
| Net income adjusted | | $ 88,315.23 |
| Less: Exemptions | | 1,200.00 |
| Balance, subject to surtax and normal tax | | $ 87,115.23 |
| One-half of $87,115.23 | | $ 43,557.62 |
| Tentative surtax | $20,888.03 | |
| Tentative normal tax at 3% | 1,306.73 | |
| Total | $22,194.76 | |
| Less reduction under Sec. 12(c), I.R.C. | 2,683.37 | |
| Total normal tax and surtax on one half of net income | | $ 19,511.39 |
| Combined normal tax and surtax ($19,511.39X2) | | $ 39,022.78 |
| Correct income tax liability | | $ 39,022.78 |
| Income tax liability shown on return account No. 9179696 | | $ 9,622.90 |
| Deficiency of income tax | | $ 29,399.88 |

[Endorsed]: T.C.U.S. Filed Aug. 8, 1951.

[Title of Tax Court and Cause.]

## ANSWER

Comes now the Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed in the above-entitled appeal, admits and denies as follows:

1, 2 and 3. Admits the allegations contained in paragraphs 1, 2 and 3 of the petition.

4.(a) Denies that respondent's determination is based upon errors as alleged in subparagraph (a) of paragraph 4 of the petition.

5.(a) Admits duplexes were transferred by the Artcraft Builders, Inc., to the petitioners and two other individuals, each individual taking an undivided one-fourth interest. Denies all remaining allegations contained in subparagraph (a) of paragraph 5 of the petition.

(b) Denies the material allegations of fact contained in subparagraph (b) of paragraph 5 of the petition.

(c) Admits returns were filed (on Form 1065), under the name of "Edward Pool & Associates" (for certain years), but denies the remaining allegations contained in subparagraph (c) of paragraph 5 of the petition.

(d) Admits duplexes of petitioners and others were sold, but denies the remaining allegations of fact contained in subparagraph (d) of paragraph 5 of the petition.

(e) Admits petitioners reported sales of the

duplexes in their 1948 return as long-term capital gains, but denies the income from said sales was properly reported, and denies further all remaining allegations of fact contained in subparagraph (e) of paragraph 5 of the petition.

6. Denies generally and specifically each and every allegation contained in the petition not hereinbefore expressly admitted, qualified or denied.

Wherefore, it is prayed that the petitioners' appeal be denied and that the Commissioner's determination be approved.

/s/ CHARLES OLIPHANT
Chief Counsel, Bureau of Internal Revenue.

Of Counsel:

B. H. Neblett, Division Counsel.

E. C. Crouter, Donald P. Chehock, Special Attorneys, Bureau of Internal Revenue.

[Endorsed]: T. C. U. S. Filed Oct. 4, 1951.

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[Title of Tax Court and Causes Nos. 36108, 36109, 36110, 36111, 36112, 36113, 36114.]

## MINUTES OF PROCEEDINGS

Date: Dec. 3, 1952. Place: Los Angeles, Calif.

Proceeding: Edward and Lottie Pool and Associated Cases.

Assigned to Judge Raum, Division No. 11.

Counsel: For Petitioner: Irving Axelrad, Esq., 6399 Wilshire Blvd., L. A., Calif. For Respondent: Charles Chase, Esq.

Stenographic Reporter: D. Cram.

Hearing: CC. Transcript Ordered: No.

On motion of Petitioner to continue proceedings to a later Los Angeles, California.

Ordered: Motion granted. Continued generally.

Filed at hearing: Motion for continuance. Appearance of Axelrad in all dockets.

Statement

/s/ CORRIE E. JONES,
Deputy Clerk

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[Title of Tax Court and Causes Nos. 36108, 36109, 36110, 36111, 36112, 36113, 36114.]

MINUTES OF PROCEEDINGS

Date: Feb. 27 and Mar. 2, 3, 4, 1953. Place: Los Angeles, Calif.

Proceedings: Edward Pool and Lottie Pool, et al.

Assigned to Judge Bolon B. Turner, Div. No. 8.

Counsel: For Petitioner: Irving I. Axelrad, Esq., 6399 Wilshire Blvd., Los Angeles 48, Calif. For Respondent: Donald P. Chehock, Esq.

Stenographic Reporter: Cram, Murdock, Trainor.

Hearing: Time: Feb. 27, 3:05 to 5:05; Mar. 2: 10:10 to 12:30, 2:00 to 5:00; Mar. 3: 10:32 to 12:35, 2:05 to 4:55, Mar. 4: 10:24 to 1:00.

Sub. —

Transcript Ordered: Yes.

On the merits: Yes.

Ordered: Pets. motions to file amended petitions in No. 36109-10-11-12, 361114, Granted; Amended Petitions filed. Served. Respondent filed Answers thereto. Served.

Stipulation of Facts, with Exhibits A-1 through 18-R.

Petitioner's brief: June 4, 1953; Reply Brief: September 17, 1953.

Respondent's brief: June 4, 1953; Reply Brief: September 17, 1953.

Witnesses for Petitioner: William K. Murphy, Thomas H. Block, Cyrus Edward LaBree, Philip Pierre Boland, Erwin Lampe, Ruby Jean Woodruff, Edward Pool.

Exhibits: Petitioner's: 19. FHA Sub-Div. Inf. Form, Tract 11674; 20. FHA Sub-Div. Inf. Form, Tract 11451; 21. Minutes, Bd. Drs. 8-18-41; 22. Minutes, Bd. Drs.—Spec. Meeting 2-17-43; 23. Security Deposits List—Tracts 11451 and 11674 (10 sheets); 24. Corporation Grant Deed; 25. Tentative Map; 26. Letter—1-4-45 (carbon copy); 27. Letter —1-9-45 (carbon copy); 28. FHA Infor. Form; 29. Letter—7-9-43 (carbon copy—2 pgs.); 30. NHA General Order No. 60-3C.

Exhibits: Respondent's: S. 1955 Partnership Return; T. 1946 Partnership Return; U. 1947 Partnership Return; V. 1948 Partnership Return; W. 1949 Partnership Return; X. 1950 Partnership Return;

Y. 1941 Corporation Return; Z. 1942 Corporation Return; AA. 1943 Corporation Return; BB. 1944

Corporation Return; CC. 1945 Corporation Return; DD. 1946 Corporation Return; EE. 1947 Corporation Return; FF. 1948 Corporation Return;

GG. 1943 Return—Edna Murphy; HH. 1944 Return—Wm. K. Murphy; II. 1945 Return—Wm. K. Murphy; JJ. 1946 Return—Wm. K. Murphy; KK. 1947 Return—Wm. K. Murphy.

LL. 1948 Return—Wm. K. and Edna Murphy.

MM. 1943 Return—Edward Pool; NN. 1944 Return—Edward Pool; OO. 1945 Return—Edward Pool; PP. 1946 Return—Edward Pool; QQ. 1947 Return—Edward Pool;

RR. 1948 Return—Edward and Lottie Pool; SS. 1949 Return—Edward and Lottie Pool; TT. 1950 Return—Edward and Lottie Pool; UU. Tentative Map; VV. Escrow Papers—70 Duplexes (6 docs.); WW. Escrow Papers—100 Duplexes (7 docs.); XX. Vet. Adm. Appraisal Report; YY. Affidavit of Publ. and 2 ads—L. A. Times 8-11-46;

ZZ. Newspaper ads—L. A. Her-Exp. 8-10-46; AAA. Newspaper ads—L. A. Her-Exp. 8-31-46; BBB. Newspaper ad—L. A. Her-Exp. 5-4-46; CCC. Newspaper ads—L. A. Her-Exp. 5-11-46; DDD. Newspaper ads—L. A. Her-Exp. 5-18-46; EEE. Newspaper ad—L. A. Exam. 5-19-46; FFF. Newspaper ads—L. A. Exam. 9-1-46;

GGG. Letter—9-18-46 (Original); HHH. Record Card; III. Analysis of leases—Tract 13163 (5 sheets).

/s/ KATHRYN L. PETERS,
Acting Deputy Clerk

The Tax Court of the United States

No. 36108—Edward Pool and Lottie Pool, Petitioners, vs. Commissioner of Internal Revenue, Respondent.

No. 36109—Edward Pool, Petitioner, vs. Commissioner of Internal Revenue, Respondent.

No. 36110—Lottie Pool, Petitioner, vs. Commissioner of Internal Revenue, Respondent.

No. 36111—William K. Murphy, Petitioner, vs. Commissoner of Internal Revenue, Respondent.

No. 36112—Edna Murphy, Petitioner, vs. Commissioner of Internal Revenue, Respondent.

No. 36113—William K. Murphy and Edna Murphy, Petitioners, vs. Commissioner of Internal Revenue, Respondent.

No. 36114—Artcraft Builders, Inc., Petitioner, vs. Commissioner of Internal Revenue, Respondent.

## STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the facts hereinafter stated are true and correct, but without prejudice to the right of either party to introduce upon the trial of this case any other and further evidence not inconsistent with the fact herein stipulated:

1. Edward Pool and Lottie Pool are husband and wife. At all times herein material, they filed their federal income tax returns on a cash and calendar year basis with the Collector of Internal Revenue for the Sixth District of California. Separate returns were filed for the years 1946 and 1947 but joint returns were filed for the year 1948.

2. William K. and Edna Murphy are husband and wife. At all times herein material, they filed their returns on a cash and calendar year basis with the Collector of Internal Revenue for the Sixth District of California. In 1946 and 1947 each filed separate returns. In 1948, however, they filed joint returns.

3. Artcraft Builders, Inc. (hereinafter referred to as Artcraft) is a California corporation. Until 1944 its principal place of business was at Los Angeles, California. Since 1945 its principal place of business has been at Long Beach, California. At all times herein material, it kept its books on the accrual and calendar year basis, and filed its returns with the Collector of Internal Revenue for the Sixth District of California, at Los Angeles, California.

4. Artcraft was organized as a California corporation on March 10, 1941. Four thousand shares of Class A preferred stock and 21,000 shares of Class B Common were authorized. Class A and Class B stock were entitled to equal voting rights, share for share. The Class A shares carried the right to cumulative dividends at the rate of 8 per cent.

5. On incorporation, 800 of the Class A shares were issued to R. T. Cooke and Mary Cooke and the remaining 3,200 shares were issued to J. S. A. Smith and Gertrude C. Smith. The Class B shares were issued as follows: 200 shares to R. T. & Mary Cooke; 800 shares to J. S. A. & Gertrude C. Smith; 1,000 shares to Edward Pool; 1,000 shares to William K. Murphy.

6. In April, 1943, an additional 25,000 shares of Class B stock were authorized and issued as follows: Edward Pool, 8,400; William K. Murphy, 8,300; J. S. A. Smith, 6,600; R. T. Cooke, 1,700.

7. On or about June 1, 1943 William K. Murphy and Edward Pool and their wives, purchased all of the stock held by Mr. & Mrs. J. S. A. Smith and Mr. & Mrs. Cooke. On June 8, 1943 Smith and Cooke resigned as officers and directors of Artcraft.

8. At all times thereafter Mr. & Mrs. Pool and Mr. & Mrs. Murphy have been the sole stockholders of Artcraft. From that date the Pools have owned 14,050 shares of the Class B stock as community property and the Murphys have owned 13,950 shares of Class B stock as community property. Each couple has from that time owned 2,000 shares of Class A stock as community property.

9. Edward Pool and Lottie Pool paid a total of $16,000.00 for all of their stock in Artcraft, and William K. Murphy and Edna Murphy paid a total of $16,000.00 for all of their stock in Artcraft.

10. In 1941, Artcraft constructed houses under individual building contracts for others. In 1942 Artcraft had some income from contracts with outsiders, but the major portion of its income was derived from building houses for sale on its own account. In 1942 Artcraft built for sale on its own account and sold 142 houses in Tract No. 12951, Los Angeles County. In 1943 Artcraft built for sale on its own account and sold 2 houses in Tract 12951, 86 houses in Tract 12287, and 100 houses in Tract 12288, all Tracts being located in Los Angeles

County, California. No income was derived by Artcraft in 1943 from building on contracts for others.

11. On February 24, 1943 Artcraft made application with the Federal Housing Administration (of the War Production Board) to build for war housing 22 structures (containing 68 units) in Tract No. 11674, and on May 26, 1943 made application to build 70 duplexes (containing 140 units) in Tract No. 11451. Attached hereto and made a part hereof are the approved applications for priorities on the two projects, marked Exhibit A-1 and Exhibit B-2, respectively. These projects were financed through FHA Title VI loans, with the Western Federal Savings and Loan Association of Los Angeles.

12. Attached hereto and made a part hereof are the minutes of Artcraft's Board of Directors dealing with Lots 1 to 22, inclusive, of Tract 11674 and Lots 1 to 70, inclusive, of Tract 11451, being the minutes of September 16, 1943, marked Exhibit C-3, the minutes of October 23, 1943, marked Exhibit D-4, and the minutes of March 31, 1944, marked Exhibit E-5. Declaration of Restrictions for Tract No. 11451, marked Exhibit F-6, and made a part hereof was executed by Artcraft, through its officers, Edward Pool and W. K. Murphy, on October 14, 1943 and recorded on October 15, 1943, with the County Recorder of Los Angeles County. Deeds to Lots 1 to 22, inclusive, of Tract 11674 and Lots 1 to 70, inclusive, of Tract 11451, with improvements, were made by Artcraft and delivered on or about March 31, 1944, to Edward Pool, Lottie Pool, William K. Murphy and Edna M. Murphy, as

tenants in common, the grantees acquiring an undivided one-fourth interest each. The lots in Tract No. 11674 and lots in Tract No. 11451, with improvements, were transferred to the four stockholders of Artcraft at cost to the corporation. On the 22 lots in Tract 11674 the improvements consisted of 5 two-family units, 10 three-family units, and 7 four- family units. On the 70 lots in Tract 11451 there were erected 70 duplexes (140 units). The 70 duplexes each contained total floor space of 1,500 square feet or 750 square feet in a dwelling unit. The 68 dwelling units in Tract No. 11674 and 70 duplexes in Tract No. 11451 were rented upon completion.

13. The four individuals, Edward Pool, Lottie Pool, William K. Murphy and Edna Murphy, on or about April 1, 1944, formed a joint venture (or partnership) known as "Edward Pool and Associates" (hereafter referred to as "Associates"). Thereafter Associates kept its books on the accrual method and fiscal year basis ending January 31st of each year.

14. Artcraft performed the services of rental agent for Associates for the period Associates owned the aforesaid properties together with 100 duplexes and a market building both referred to hereinafter. As rental agent Artcraft entered into leases, collected rents, kept books, paid bills and generally managed the property. For these services Associates paid Artcraft the following amounts: "1944, $7,745.88; 1945, $9,357.60; 1946, $23,614.44; 1947,

$15,500.00; 1948, $12,000.00; 1949, $12,000.00." Similar form leases were used for each unit in Tracts 11451, 11674 and 13163 (100 duplex project hereafter mentioned). Attached hereto, marked Exhibit G-7 and made a part hereof, is a typical form lease used for these three projects.

15. Attached hereto, market Exhibits H-8(a) to (d), inclusive, and made a part hereof, are National Housing Administration Orders Nos. 60-1, 60-2, 60-3, and 60-3B applicable to the projects here involved in Tracts 11451, 11674 and 13163. All dwelling units here involved were subject to rent control during the taxable years. Permission was obtained for rentals charged from the proper governmental agency.

16. The cost of Tracts 11451 and 11674, with improvements, to Arteraft, can be summarized as follows:

| | |
|---|---|
| Cost of Tract 11451 to Arteraft: | |
| Land and subdivision costs | $ 45,800.63 |
| Buildings | 432,147.11 |
| Total | $477,947.74 |

Arteraft received FHA insured loans, through Western Federal Savings and Loan Association, of $525,000.00 on Tract 11451 and executed Trust Deeds for same. The property was thereafter, on or about March 31, 1944, transferred to the four stockholders for $477,947.74, being the cost of the property to the corporation. The difference between the $525,000.00 and $477,947.74, or $48,052.26 was then made available by credit entries to Associates.

| | |
|---|---|
| Cost of Tract 11674 to Artcraft: | |
| Land and subdivision costs | $ 26,842.97 |
| Buildings | 202,139.75 |
| Total | $228,982.72 |

Artcraft received FHA insured loans, through the same loan association, of $212,614.41 on this Tract 11674 and executed Trust Deeds for same. The property was thereafter on or about March 31, 1944, transferred to the four stockholders for $228,-982.72, being the cost of the property to the corporation.

17. In the audit of the four individual returns for 1944, the revenue agent proposed deficiencies based on his conclusion that the property comprising Tract 11451 and also Tract 11674 had been transferred by Artcraft to its stockholders at an amount less than the fair market value of the property. The difference between the transfer price and fair market value, the revenue agent concluded, constituted a dividend to the individuals. This issue was settled by agreement that the individuals had received a dividend totaling $30,149.36, of which $20,776.82 applied to Tract 11451 and $9,372.54 applied to Tract 11674. The basis of the property was then increased by the individuals by the amount of the dividend for purposes of determining depreciation and gain from the property when sold.

In 1946 deficiency notice of Artcraft the net operating loss carry forwarded from the year 1944 has been adjusted by increasing the income of Artcraft corporation by the $30,149.36, which represents the difference between the transfer price to the stock-

holders and the respondent's determined fair market value.

18. Artcraft's earnings and profits, per its books, are as follows:

| | | |
|---|---|---|
| Earnings and Profits to 12/31/41 | Loss | $(11,705.52) |
| Earnings and Profit—Year 1942 | $3,190.15 | |
| Preferred Stock Dividend Paid | (480.00) | 2,710.15 |
| Deficit in earnings and Profits at 12/31/42 | | $( 8,995.37) |
| Earnings and Profit—Year 1943 | $27,275.34 | |
| Less Federal Income Tax | (4,965.19) | 22,310.15 |
| Earnings and Profits (per books) at 12/31/43 | | $ 13,314.78 |
| Adjustments recorded on books to reflect Revenue Agent's Examination (report 8/29/44): | | |
| Add: Last month's rental deposits to income earned in 1943 | | 1,786.78 |
| Professional expenses transferred to Incorporation Expense | | 143.93 |
| | | $ 15,245.49 |
| Less: Additional 1943 Income Tax | | 521.30 |
| Adjusted Earnings and Profits at 12/31/43 | | $ 14,724.99 |
| Dividends on Preferred Stock—1944 | | (480.00) |
| Loss from Operations during 1944 | | *(44,060.59) |
| Earnings and Profits 12/31/44—Deficit | | *(29,816.35) |
| Refund of 1943 Income Tax (carryback) | | 5,486.49 |
| | | $(24,329.86) |
| Loss from Operations during 1945 | | (8,076.15) |
| Deficit in Earnings and Profits at 12/31/45 | | $(32,406.01) |
| Earnings and Profits for 1946 | $36,479.00** | |
| Less Provision for Federal Income Taxes | (1,057.59) | |
| Less Preferred Stock Dividends | (640.00) | |
| Net earnings and Profits for 1946 | | 34,781.41 |

| | |
|---|---|
| Earnings and Profits at 12/31/46 | $ 2,375.40 |
| In 1946 organization expense was written off against accumulated earnings in the amount of.... | 383.82 |
| Earnings and Profits 12/31/46 | **$ 1,991.58 |

* These figures disregard the $30,149.36 additional income respondent concluded was earned by Artcraft in 1944 by transferring property to its stockholders for $30,149.36 less than its alleged fair market value. By this adjustment in 1944 the loss from operations in 1944 would be $13,911.23 instead of $44,060.59. By virtue of the $30,149.36 distribution to stockholders in 1944, the deficit of the corporation on 12/31/44 is the $29,816.35 shown above.

** These figures disregard the $100,464.98 additional income respondent has determined was earned by Artcraft in 1946 by the sale of property to its stockholders for $100,464.98 less than the fair market value. By this adjustment in 1946 the earnings and profits in 1946 would be $136,943.98 instead of $36,479.00. By virtue of the $100,464.98 distribution to the stockholders, the earnings and profits of the corporation on December 31, 1946 is the $1,991.58 shown above. This $1,991.58 does not reflect the contested tax deficiency respondent is asserting against the corporation for 1946.

19. During 1944, Artcraft built a market building on a lot owned by Associates located at the southwest corner of Lakewood Boulevard and Stearns Street, Long Beach, California. Attached hereto, marked Exhibit I-9, and made a part hereof, is a copy of the minutes of the corporation's Board of Directors of June 14, 1944, relating to the market building. The market building was constructed for the stockholders at the corporation's cost, plus 10 per cent. The completed cost of this market building to Associates was $51,409.95. Associates still own the building. At all times since completion, the building has been rented.

20. Attached hereto and made a part hereof

are the minutes of Artcraft's Board of Directors dealing with Lots 1 to 100, inclusive, in Tract 13163, being the minutes of February 26, 1945, marked Exhibit J-10, the minutes of February 1, 1946 marked Exhibit K-11, and the minutes of August 26, 1946 marked Exhibit L-12. A Declaration of Restrictions for Tract 13163, exact in form to Exhibit 6-F except for the date and description, was executed by Artcraft, through its officers Edward Pool and W. K. Murphy on February 26, 1945 and recorded on March 9, 1945. The 100 duplexes were constructed, and deed to Lots 1 to 100, inclusive, of Tract 13163, with improvements, was made by Artcraft, bearing date of March 21, 1946, to W. K. Murphy, Edna Murphy, Edward Pool and Lottie Pool, as tenants in common, the grantees acquiring an undivided one-fourth interest each. This deed was recorded in the office of the County Recorder, Los Angeles County, California, on May 16, 1946. The property was transferred to the stockholders for the actual cost to the corporation for the land and improvements plus an additional amount of $35,333.21. The transfer price of the property to the stockholders is summarized as follows:

| | |
|---|---|
| Land and subdivision costs to Artcraft | $ 63,013.81 |
| Building cost to Artcraft | 525,873.00 |
| Additional payment by stockholders to Artcraft | 35,333.21 |
| Total | $624,220.02 |

The $624,220.02 is the cost basis used by the Associates in reporting gain from the sale of the 100 duplexes in Tract 13163.

Artcraft received FHA insured loans, through the Western Federal Savings and Loan Association, on this Tract 13163 aggregating $724,685.00. The difference between the $724,685.00 and $624,220.02, or $100,464.98, was then transferred by credit entries to the stockholders.

21. Attached hereto, marked M-13, and made a part hereof is the approved application for priorities of the 100 duplex project in Tract No. 13163 made by Artcraft on January 4, 1945. The 100 duplexes constructed by Artcraft prior to its transfer to the stockholders, each contained floor space of 1,540 square feet, or 770 square feet in a dwelling unit.

22. The 70 duplexes in Tract 11451 were sold in 1946 as shown by Exhibit N-14 attached hereto and made a part hereof. The 100 duplexes in Tract 13163 were sold in 1946 and 1947 as shown by Exhibit O-15 attached hereto and made a part hereof. The profits from the 70 duplexes in Tract 11451, and profits from 65 of the duplexes in Tract 13163, were reported by the Associates on Form 1065 for the fiscal year ended January 31, 1947. Profits from 34 of the duplexes in Tract 13163, sold in the period from February to July, 1947, were reported by the Associates on Form 1065 for the fiscal year ended January 31, 1948. These profits, from sale of the 70 duplexes in Tract 11451, and sale of the 100 duplexes in Tract 13163, were treated by the Associates on the Forms 1065, and by the petitioners Edward Pool, Lottie Pool, William K. Murphy and

Edna Murphy, in their individual returns, as long-term capital gains.

23. Attached hereto and made a part hereof are the following exhibits showing an analysis of the rental and sales income of the Associates for each respective period, to-wit: Exhibit P-16, for the period from April 1, 1944 to January 31, 1945, and also for the fiscal year ended January 31, 1946; Exhibit Q-17 for the fiscal year ended January 31, 1947; and Exhibit R-18 for the fiscal year ended January 31, 1948.

24. The 22 multiple houses in Tract 11674 were sold during the calendar years 1949 and 1950. Sale of the 1 remaining duplex in Tract 13163 was completed on February 28, 1949. The gross, cost, and net profit from sales of the 22 multiple houses in Tract 11674, per the returns filed by Associates, may be summarized as follows:

| | | | |
|---|---|---|---|
| Gross sales—fiscal year ended January 31, 1950 | | | $133,938.94 |
| Basis of property sold: | | | |
| Land | $ 12,387.99 | | |
| Buildings | 89,489.49 | | |
| | $101,877.48 | | |
| Less depreciation | 24,459.70 | | |
| | | $ 77,417.78 | |
| Commisions paid Real Estate Agent | | 5,336.29 | |
| Loan prepayment bonus | | 215.00 | |
| Escrow costs | | 917.24 | |
| | | | 83,886.31 |
| Profit from sales | | | $ 50,052.63 |
| Gross sales—fiscal year ended January 31, 1951 | | | $171,750.00 |

| | | | |
|---|---|---|---|
| Basis of property sold: | | | |
| Land | $ 14,454.98 | | |
| Buildings | 122,022.80 | | |
| | $136,477.78 | | |
| Less depreciation | 36,669.58 | | |
| | | $ 99,808.20 | |
| Commissions | | 7,073.30 | |
| Other charges | | 2,506.51 | |
| | | | $109,388.01 |
| Profit from sales | | | $ 62,361.99 |

/s/ IRVING I. AXELRAD
Counsel for Petitioners
/s/ CHARLES W. DAVIS
Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent

[Endorsed]: T.C.U.S. Filed Feb. 27, 1953.

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T. C. Memo. 1956-64

The Tax Court of the United States

EDWARD POOL and LOTTIE POOL, et al.,[1] Petitioners, vs. COMMISSIONER OF INTERNAL REVENUE, Respondent.

## FINDINGS OF FACT AND OPINION

Docket Nos. 36108, 36109, 36110, 36111, 36112, 36113, 36114. Filed March 20, 1956.

In 1946 a corporation transferred 100 duplexes,

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[1] The proceedings of the following petitioners are considered herewith: Edward Pool, Docket No.

the construction of which it had financed through F.H.A. insured loans, to its four stockholders, subject to the encumbrances thereon, none of which were in any way or to any extent assumed by them but in respect of which they were to account to the corporation from rents received thereon and from proceeds of sales or other hypothecation for the amounts necessary to cover the maturities on the said encumbrances. The aggregate of the F.H.A. insured loans received by the corporation had exceeded the cost of the duplexes by $135,798.19, and of that excess the corporation likewise distributed to its four stock holders $100,464.98 in cash. At January 1, 1946, the corporation had no accumulated earnings, but for 1946, after the payment of dividends on preferred stock and provision for Federal income taxes, it had net earnings of $34,781.41. The respondent determined that the fair market value of the duplexes at the time of transfer exceeded "the total consideration received therefor" by $100,464.98, and that both the corporation and the stockholders received income in that amount. Held, that in the distribution of the duplexes by the corporation to its stockholders, the corporation realized no taxable gain therefrom. Also, held, that by reason of the above distributions, the stockholders received a dividend of $34,781.41, the amount of the corporate net earnings for 1946, or $8,694.35 each.

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36109; Lottie Pool, Docket No. 36110; William K. Murphy, Docket No. 36111; Edna Murphy, Docket No. 36112; William K. Murphy and Edna Murphy, Docket No. 36113; and Arteraft Builders, Inc., Docket No. 36114.

and that the excess of the distributions over and above the amount of such net profits are, under section 115 (d) of the Internal Revenue Code of 1939, to be applied against and reduce the basis to the stockholders of their corporate stock and any excess over and above such basis is taxable in the same manner as gain from the sale or exchange of property.

In 1944 the corporation had similarly made transfers to its four stockholders of 22 apartment buildings and 70 duplexes, together with the cash representing the excess of the F.H.A. insured loans relating to the 70 duplexes over its cost thereof. Based on a determination that the corporation had realized gain on the distribution of the said properties to its stockholders, the respondent disallowed for 1946 a 1944 net loss carry-over. Held, that the respondent erred in determining that the corporation realized gain upon the transfer of the properties to its stockholders.

As the apartment buildings and the duplexes had been completed, they had been rented, and the rental thereof was continued after their distribution to the stockholders. Within months after the transfer of the 100 duplexes in 1946, the stockholders, taking into account the market for such housing, the profits which could be realized and other factors, decided to sell the entire 170 duplexes which had been so distributed to them and employed an experienced real estate broker for that purpose, for a flat compensation of $500 per duplex. The stockholders supplied the necessary office facilities, in-

cluding telephone, and some clerical and stenographic services; and one of the stockholders worked out problems of financing for purchasers. The real estate broker wrote the copy for the advertising, employed some sales assistance and some office help, paying for these services and advertising on his own account. An aggressive and active sales campaign was conducted, and within twelve to fifteen months, all of the duplexes, except one, had been sold. Held, that the duplexes sold were not property used by the stockholders in their trade or business, within the meaning of section 117 (j) of the 1939 Code, but were property held by them primarily for sale to customers in the ordinary course of their selling business, within the meaning of section 117 (a), and that the gain realized was not capital gain, but ordinary income.

Irving I. Axelrad, Esq., for the petitioners.

Donald P. Chehock, Esq., for the respondent.

Turner, Judge: The respondent determined deficiencies in income tax against the petitioners as follows:

| Docket No. | | Year | Deficiency |
|---|---|---|---|
| 36108 | Edward Pool and Lottie Pool | 1948 | $ 29,399.88 |
| 36109 | Edward Pool | 1946 | 12,919.82 |
| | | 1947 | 100,829.79 |
| 36110 | Lottie Pool | 1946 | 12,919.82 |
| | | 1947 | 100,829.78 |
| 36111 | William K. Murphy | 1946 | 12,569.14 |
| | | 1947 | 112,359.85 |
| 36112 | Edna Murphy | 1946 | 12,569.13 |
| | | 1947 | 112,359.84 |
| 36113 | William K. Murphy and Edna Murphy | 1948 | 28,207.82 |
| 36114 | Artcraft Builders, Inc. | 1946 | 48,814.50 |

The questions for decisions are (1) whether in 1944 and 1946 Artcraft Builders, Inc., realized gain as the result of transfers or distributions made by it to its stockholders; (2) whether, by reason of the transfers or distributions in 1946, the stockholders received income; and (3) whether in the selling of 170 duplexes which had been transferred or distributed to them in the years above, the stockholders were selling property held by them primarily for sale to customers in the ordinary course of their business, to the end that the gain realized was not capital gain, as claimed by them, but ordinary income.

## Findings of Fact

Some of the facts have been stipulated.

Edward Pool and Lottie Pool are husband and wife. They filed their income tax returns on a cash basis and by calendar years, and their returns for the years herein were filed with the collector of internal revenue for the sixth district of California. For the years 1946 and 1947 they filed separate returns. For the year 1948 they filed a joint return.

William K. Murphy and Edna Murphy are husband and wife. They filed their returns on a cash basis and by calendar years, and their returns for the years herein were filed with the collector of internal revenue for the sixth district of California. For the years 1946 and 1947 they filed separate returns. For the year 1948 they filed a joint return.

Artcraft Builders, Inc., sometimes referred to as Artcraft, is a California corporation. Until 1944, its principal place of business was in Los Angeles.

Since 1945 its principal place of business has been in Long Beach. At all times material herein it kept its books on an accrual basis and filed its income tax returns for calendar years with the collector of internal revenue for the sixth district of California.

Artcraft was organized on March 10, 1941. Its authorized capital stock consisted of 4,000 shares of Class A preferred stock and 21,000 shares of Class B common stock. Both classes of stock had voting rights share for share. The Class A shares carried the right to cumulative dividends at 8 per cent. At the time of incorporation the 4,000 shares of Class A stock were issued, 800 shares to R. T. Cooke and Mary Cooke and 3,200 shares to J.S.A. Smith and Gertrude C. Smith. Of the Class B common stock, 3,000 shares were issued, 200 shares to R. T. and Mary Cooke; 800 shares to J. S. A. and Gertrude C. Smith; 1,000 shares to Edward Pool and 1,000 shares to William K. Murphy.

Artcraft was organized to engage in residential building construction. During 1941 most, if not all, of its business was that of constructing houses under contract for others. During 1942 the major portion of its income was derived from building houses for sale for its own account, although it did have some income from building contracts. In 1942 it built for sale on its own account and sold 142 houses in Los Angeles County. In 1943 it built for sale on its own account and sold 188 houses, all of which were likewise located in Los Angeles County.

It derived no income in 1943 from building under contract for others.

Edward Pool was named president of Arteraft. He had been a builder during all of his business life. Prior to 1935, when he moved to Long Beach, he had lived in Cincinnati, Ohio, and had built houses in that area. During the period of his operations in the Cincinnati area and after moving to Long Beach, but prior to the organization of Arteraft, he had built houses both for sale on his own account and for others under contract. He had never built rental houses for his own account. Throughout his operations he sold all of his houses through brokers. He never had a real estate broker's license and never sold any houses personally.

William K. Murphy moved to California from Illinois in 1933. Prior to that time he had been variously employed. For a short period he had done office work for a concern which built houses. About 1938 he started working as an employee of "Pacific Construction and Finance." While with that concern he worked on "rough drafts of sketches of apartment buildings and home layouts." This work continued until he became connected with Arteraft. He had never sold real estate or had a real estate broker's license. According to the corporate minutes, his employment with Arteraft in 1942 was that of sales manager.

At a meeting of the board of directors of Arteraft held on August 18, 1942, Murphy reported that 24 houses had been "sold to date." Action was taken to increase loans on 126 houses then under

construction and to proceed with plans for the construction of 86 more houses. Pool "brought up the question of building 27 income units in addition, but this proposal was turned down."

At a special meeting of the board of directors of Artcraft held on February 17, 1943, Pool reported that sales had been made of 36 houses under construction in a designated tract; that all foundations and rough carpenter work had been completed on 86 houses; and that arrangements would be made to start work on 100 houses in another tract. Pool "also reopened the subject to building residential income in two, three and four unit apartments. The subject was discussed and decided not to take any action at this time, but to hold it open for future consideration."

On February 24, 1943, Artcraft made application to the Federal Housing Administration of the War Production Board to build for war housing 22 multiple dwelling structures, containing 68 family units, in Tract No. 11674, and on May 26, 1943, made application to build 70 duplexes, containing 140 units, in Tract No. 11451, both tracts being located near Long Beach and the Douglas Aircraft plant. These projects were to be, and were financed through F.H.A. Title VI loans with Western Federal Savings and Loan Association of California. As a part of its application in each instance. Artcraft agreed that it would hold for rent the accommodations contemplated at rentals per unit not in excess of monthly charges designated in the application, except as otherwise authorized by General Orders

60-2 and 60-3 of the National Housing Agency, and that it would not include in the lease of said accommodations any option to purchase except in accordance with said general orders; and further, that, except as authorized by the said general orders, it would not otherwise dispose of or enter into any agreement or contract for the disposal of any of the said accommodations, or any title interest, and that it would notify any transferee of the said accommodations that he must comply with the provisions of the said general order relative to occupancy.

In April of 1943, 25,000 additional shares of Artcraft Class B common stock were authorized and issued, 8,400 shares to Edward Pool, 8,300 shares to William K. Murphy, 6,600 shares to J.S.A. Smith and 1,700 shares to R. T. Cooke.

Subsequently, and on or about June 1, 1943, William K. Murphy and Edward Pool and their wives purchased all of the Artcraft stock held by the Smiths and Cookes.[1] and on June 8, 1943, Smith and Cooke resigned as officers and directors of the company. At all times thereafter, Edward Pool, Lottie Pool, William K. Murphy and Edna Murphy have been the sole stockholders of Artcraft, the Pools owning 14,050 shares of Class B stock as community property and the Murphys owing 13,950 shares of such stock as community property. Each couple from that date has owned 2,000 shares of the Class

[1] It was the testimony of both Pool and Murphy that neither Smith nor Cooke desired to engage in the construction of rental housing.

A preferred stock as community property. The cost to each couple for all of the shares owned by them was $16,000.

The application, filed on February 23, 1943, for approval of the proposed construction of 22 multiple dwelling units on Tract 11674, was approved by the Federal Housing Administration on June 1, 1943, and by the War Production Board on June 7, 1943. The application, filed on May 26, 1943, for approval of the proposed construction of 70 duplexes on Tract No. 11451, was approved by the Federal Housing Administration on June 7, 1943, and by the War Production Board on June 16, 1943.

General Orders 60-2 and 60-3 were part of the Operating Manual, National Housing Agency, General Order No. 60-2 being designated "Public Regulations—Occupancy and Disposition of Private War Housing," and General Order No. 60-3, as "Public Regulations — Methods of Disposition of Private War Housing Including Rent Levels, Sales Prices, and Petitions to the National Housing Agency."

General Order 60-2 recited that the National Housing Agency was responsible for the proper occupancy of housing programmed for war workers and for the adoption of regulations assuring that war housing would be held available for eligible war workers for the duration of the national emergency declared by the President on September 8, 1939. Under the order, private war housing was to be regarded as "begun" on the date of submitting to the Federal Housing Administration a properly executed application for priority assistance or authority

to begin construction in connection with such housing, and the date of "completion" was to be the date upon which such housing was offered for initial rental or sale, or the date upon which it was first ready for immediate occupancy, whichever was later. The phrase "held for rental" included "only an ordinary landlord-tenant relationship or such a tenancy coupled with an option to purchase." Under the option, the tenant was not to be obligated to purchase and the option was to run only in his behalf. The selling price was to "be a fair market price, or $6,000," whichever was lower. The option to purchase could not be exercised prior to the expiration of four months' occupancy, and was to continue for at least 30 months, unless sooner exercised. Private war housing begun on or after February 10, 1943, was to be made available for initial occupancy, and for reoccupancy, only by eligible war workers. It was provided, however, that at any time subsequent to 60 days after completion of such housing, the owner might petition the National Housing Agency to permit initial occupancy, or reoccupancy, as the case might be, by a person other than an eligible war worker. Except for involuntary transfers, private war housing could be disposed of (a) only to an occupant, after 4 months' occupancy; (b) to a person who would not himself occupy the housing, provided the occupancy and disposition limitations applicable prior to purchase or acquisition should continue to be applicable after such purchase or acquisition; or (c) at any time subsequent to 60 days after completion of any such housing, the owner

might petition the National Housing Agency to permit disposition otherwise than as indicated in (a) and (b).

General Order 60-3 was designed to implement the occupancy and disposition policies of the National Housing Agency applicable to all private war housing as stated in General Order No. 60-2. It also provided that for the duration of the national emergency declared by the President on September 8, 1939, all private war housing begun on or after February 10, 1943, should be held for rental to eligible war workers as provided in General Order No. 60-2, at the rentals specified in the application, which rentals should in no event exceed $50 per month shelter rent for one unfurnished dwelling unit, plus a reasonable charge for tenant services, which was not to exceed $3 per month per room. It also carried provision that "a dwelling unit * * * may be purchased by an occupant * * * after four months of continuous occupancy," but that the purchase price might not exceed the fair market price, or $6,000, whichever was lower. In the case of such sale, the seller was required to submit an agreement on the part of the purchaser that such purchaser would continue to occupy the dwelling unit, or would hold the unit subject to the occupancy and disposition provisions set forth in General Order No. 60-2. Subject to the same restrictions as to price, such houses could also be transferred to a person who would not become an occupant thereof, but only if an agreement was submitted stating that the housing would be held subject to the provisions

of General Order No. 60-2. Further, at any time subsequent to 60 days after completion, the original owner or a subsequent owner might petition the National Housing Agency to permit disposition otherwise than as provided above.

General Order No. 60-3 was thereafter superseded by General Orders Nos. 60-3A, 60-3B, which became effective August 25, 1943, and 60-3C, which became effective November 12, 1943. In so far as appears, the superseding orders were, for the purposes here, substantially the same as General Order No. 60-3.

At a special meeting of Arteraft's board of directors held on September 16, 1943, Pool stated that he and Mrs. Pool and Murphy and Mrs. Murphy desired "to take over" the title to and become the owners of the 22 lots in Tract 11674 and the 70 lots in Tract 11451, together with all buildings then erected and those to be erected thereon, that they desired to take title as tenants in common, each owning an undivided one-fourth interest therein, and in addition, that moneys obtained from loans thereon over and above actual cost should likewise be transferred to them as tenants in common, "in consideration of which the corporation should retain all rentals and/or payments received upon any of said buildings up to the time of such take-over, and further, that while he, William K. Murphy, Edna Murphy and Lottie Pool would assume no personal responsibility they would nevertheless agree that so long as rentals or sales of said properties produced sufficient funds, that of such funds as received a

portion thereof would be paid over to persons, firms or corporations holding encumbrances against said properties sufficiently to liquidate payments upon said encumbrances as the same fell due, strictly in accordance with but not in excess of the requirements of said encumbrances, respectively, no personal obligation however being assumed by any of the above named persons." Thereafter a motion was made, and carried, wherein "it was ordered that this corporation shall and does hereby agree to sell and transfer" to the four individuals named the properties in question, according to the terms which had been outlined by Pool, and providing further for application and payment by Pool, Murphy and their wives from moneys thereafter received from "the sale, hypothecation or rentals of said properties of all sums accruing in accordance with the terms of any and all indebtedness or obligations now or hereafter existing against said properties respectively." But it was expressly provided that there was to be no personal liability on the part of the individuals, "or either of them," for payment of the "moneys owing upon said mortgages or encumbrances or the notes thereby secured other than as received from sales, hypothecation or rentals of said property and then only so much thereof as is called for in and required by said encumbrance obligations." The motion also provided for the transfer to the four individuals of all sums of money remaining in the hands of Arteraft from sums theretofore borrowed for "the purchase of said property and the erection of said buildings and

improvements thereon after deducting from said sums the actual cost of such land, buildings and improvements." A motion was next adopted that thereafter all profits from the sale, rental or hypothecation of the properties over and above the amount "of said mortgage indebtednenss" should be and remain the sole exclusive property of the four individuals as tenants in common.[3]

The total consideration for which Artcraft purchased the land known as Tract 11451 was $12,195. On some undisclosed date Pool and Murphy had each advanced $3,000 to Artcraft towards the purchase of the land in question. At a special meeting of Artcraft's board of directors on October 23, 1943, Pool brought up the matter of the loans by him and Murphy, and requested that the corporation execute to each of them its promissory note for the amount advanced. A motion was made, and carried, that the notes suggested be issued, payable 30 days from date, without interest.

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[3] At this meeting and others at which the transfer of war housing by Artcraft to its stockholders was under consideration, Pool, as president, and Murphy, as secretary, purported to resign as officers and directors of Artcraft, and individuals having no apparent interests in the corporation were purportedly elected to the said offices. Aside from the fact that one of the individuals named was an individual in attendance as counsel for Artcraft, the identity of the purported successors in office does not appear. Immediately after the adoption of the motions indicated, the ritual of accepting purported resignations of the said individuals was indulged in and Pool and Murphy purported to resume their official positions.

Generally speaking, the dwelling units on Tracts 11674 and 11451 was rented as construction was completed. The first unit to be rented was in one of the 22 apartment buildings on Tract 11674. It was rented on the day before Thanksgiving in 1943. The terms and conditions under which the said housing was rented, including rental rates, were in keeping with the requirements of General Orders Nos. 60-2 and 603. The initial leases were for a period of one year. A few of the apartments may thereafter have been leased for longer periods.

At a special meeting of Artcraft's board of directors held on March 31, 1944, Pool advised that all buildings on Tracts 11674 and 11451 would be completed by the night of that day, and that "the time had now arrived when he and Mr. Murphy, together with their respective wives, could expect the completion of the contract entered into by and between this corporation and he (sic) and Mr. Murphy and their respective wives on September 16, 1943." A motion was made, and carried, that the president and secretary be authorized, empowered and directed to "carry out the terms of the agreement entered into between this corporation and Edward Pool, Lottie Pool, William K. Murphy and Edna M. Murphy as reflected in the minutes * * * covering the meeting held September 16th, 1943, and in so doing to transfer all the title" of Artcraft in the 22 lots and building in Tract 11674 and the 70 lots and buildings in Tract 11451 to the four individuals, as tenants in common, and further, to transfer unto them all moneys theretofore obtained

by Artcraft in the form of loans upon the said property for the erection of the said buildings remaining over and above the actual costs thereof, and that the transfers be so drawn that no personal responsibility should be assumed by the four individuals, or either of them, "with reference to the payment of any obligations against said property or properties"; provided, however, that the four individuals furnish to the corporation "their written agreement that so long as rentals of said properties produce sufficient funds, that of such funds as received a portion thereof would be paid over to persons, firms or corporations holding encumbrances against said properties sufficiently to liquidate payments upon said encumbrances as the same fell due, strictly in accordance with but not in excess of the requirements of said encumbrances, respectively, no personal obligation however being assumed by any of the above named persons; all of the foregoing being subject to the provision, however, that this corporation shall retain all rentals and/or payments received upon any of said buildings up to the time of the execution of said instrument of conveyance." After the adoption of the motion, Pool, for himself and the other three stockholders, delivered an instrument whereby the four individuals agreed "that so long as rentals or sales of said properties produced sufficient funds, that of such funds as received a portion thereof would be paid over to persons, firms or corporations holding encumbrances against said properties sufficiently to liquidate payments upon said encumbrances as the same fell due,

strictly in accordance with but not in excess of the requirements of said encumbrances, respectively, no personal obligation however being assumed by any of the above named persons." According to the minutes, deeds conveying the said properties to the four individuals, "as tenants in common, each owning an undivided one-fourth interest therein, in accordance with the foregoing motion," were thereupon delivered.

The total cost to Arteraft of Tract 11451, with improvements, was $477,947.74, being $45,800.63 representing land and subdivision costs and $432,-147.11 representing cost of buildings. With respect to the said property Arteraft had received F.H.A. insured loans, through Western Federal Savings and Loan Association, of $525,000 and had executed trust deeds therefor. The difference between the cost of the properties composing Tract 11451 and the loan, or $48,052.26,[4] was made available to Pool, Murphy and their wives by credit entries.

The total cost to Arteraft of the land and buildings of Tract 11674 was $228,982.72, representing $26,842.97 as land and subdivision costs and $202,-139.75, as the cost of the buildings. The amount of the F.H.A. insured loans received by Arteraft on the said property was $212,614.41.

On or about April 1, 1944, Edward Pool, Lottie Pool, William K. Murphy and Edna Murphy

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[4] This amount is as shown by the stipulation of the parties. If, however, the amounts (also stipulated) from which this amount is derived are correct, the instant amount should read $47,052.26.

"formed a joint venture (or partnership) known as Edward Pool and Associates." Edward Pool and Associates, sometimes referred to as Associates, was formed for the purpose of holding and dealing with the properties which had been transferred by Arteraft to the said four individuals as above shown. Associates kept its books under an accrual method of accounting and on the basis of a fiscal year ending January 31. It filed partnership returns of income, Form 1065, for the fiscal years ended January 31, 1945, through January 31, 1950, inclusive.

At some time prior to June 14, 1944, Pool and Murphy began the construction of a market building on a lot owned by them and their wives in Long Beach. The actual construction work was done for them by Arteraft. There was no written contract or agreement with respect to the work Arteraft was doing, but at a special meeting of Arteraft's board of directors on June 14, 1944, after Pool had recited that Arteraft was doing the work for the individuals named "upon a basis of cost plus 10%," a motion was made, and carried, that the contract for construction of the market building in the terms stated be ratified, confirmed and approved. The completed cost of the market building to the four individuals was $51,409.95. At all times since its completion, the building has been rented, and at the time of the trial herein was still owned by the four individuals.

Under date of January 4, 1945, Arteraft made a priorities application to the National Housing Agency of the Federal Housing Administration for

the construction of 100 duplexes on Tract No. 13163 in Long Beach. As in the case of the construction heretofore described on Tracts 11674 and 11451, Artcraft, as a part of its application, represented that it would hold the proposed accommodations for rent and would rent them only to eligible war workers as defined in the National Housing Agency's General Order No. 60-1, and that any sales thereof would be only as permitted by National Housing General Orders Nos. 60-2 and 60-3; and further, that rents and other charges to tenants would not be in excess of the amounts thereafter shown in the application, which schedule indicated a charge of $42.50 as shelter rent and $7.75 as a charge for services, making a total charge of $50.25 per month. In making the application, Artcraft represented itself as the project owner. The application was approved under date of February 5, 1945. This project was financed through F.H.A. insured loans from Western Federal Savings and Loan Association aggregating $724,685.

At a special meeting of Artcraft's board of directors held on February 26, 1945, Pool stated that he and Murphy were willing to "take over" title to and become the owners of the 100 lots in Tract 13163, and desired to take such title in the names of William K. Murphy, Edna Murphy, Edward Pool and Lottie Pool, as tenants in common, each to own an undivided one-fourth interest therein, but that they desired to take title only after the buildings had been fully erected and completed and all other contemplated improvements had been made upon

the said lands; "that in consideration of said transfer the corporation should and could retain all rentals and/or payments received upon any of said buildings up to the time of such take-over, * * * until the same shall have accumulated the sum of $20,000.00 which said sum of money shall be retained by Artcraft Builders, Inc. as its consideration for this agreement and for the then transfer by Artcraft Builders, Inc. of all its right, title and interest in and to said property and in and to all funds then remaining in the hands or to the credit of said Artcraft Builders, Inc. which said funds had been borrowed, accumulated or set-aside for the construction of said buildings upon said tract." Pool then stated that he and his associates would take title subject to any and all encumbrances against the property "at the time of such take-over," but that it should be definitely understood that neither he nor any of the other grantees would assume any obligation for the liquidation of such encumbrances, but that they would agree "that so long as rentals or sales of said properties produced sufficient funds, that of such funds as received a portion thereof would be paid to persons, firms or corporations holding encumbrances against said property sufficiently to liquidate payments upon said encumbrances as the same fell due, strictly in accordance with but not in excess of the requirements of said encumbrances, respectively, no personal obligation however being assumed by any of the above-named persons." A motion was thereafter made, and carried, that Artcraft did agree to trans-

fer to the individuals named, as tenants in common, the said 100 lots of Tract 13163, "together with any and all buildings and improvements erected or to be erected thereon in accordance with the present plans of the corporation," and further, was to transfer to the four individuals, as tenants in common, all sums of money remaining in its hands from the sums borrowed for the purchase of the said property and the erection of the buildings and improvements thereon after deducting the cost of the land and the buildings and improvements, these transfers to be according to the conditions as outlined in Pool's proposal above. It was further provided that any and all profits thereafter remaining from rent, sale or hypothecation of the said properties over and above the amount of the mortgage indebtedness should be and remain the sole and exclusive profit of the four individuals.

At the regular meeting of Artcraft's board of directors held on February 1, 1946, Pool stated that all buildings and improvements on Tract 13163 were fully completed and that he, Lottie Pool, William K. Murphy and Edna Murphy "were desirous of completing the contractual relationship entered into by this corporation and Mr. Pool and the above mentioned associates on the twenty-sixth day of February, 1945." He stated that at the time of the 1945 meeting, it was then believed "that it would only be possible in the carrying out of the said transaction to permit the retention of the sum of Twenty Thousand Dollars ($20,000.00) by this corporation as a consideration passing to it for said

transfer, but that since the completion of the buildings he and his associates * * * were willing to increase the amount of said retention from Twenty Thousand Dollars ($20,000.00) to Ninety Thousand Dollars ($90,000.00)." A resolution was then adopted for the transfer of the properties by "a good and sufficient deed of conveyance." A second resolution was then proposed, and adopted, to the effect that Arteraft also transfer to the four individuals, as tenants in common, all sums of money borrowed for the purchase of the property and the erection of the buildings and improvements remaining in its hands over and above the actual cost of the land, buildings and improvements; and further, that it likewise transfer to the said individuals the sums remaining in its hands from either rentals or payments for the said property since the erection of the buildings, which up to and including the first day of February 1946, was in excess of the sum of $90,000, the $90,000 to be retained by Arteraft "as a consideration for the transfer of said property and of said sums of money so remaining from the sums borrowed for the purchase of said property and the erection of said buildings and improvements thereon." The resolution also provided that it should be "expressly recognized that no personal liability" was then or at any other time assumed or intended to be assumed by the four transferees for the payment of any sums of money owing upon any mortgages, encumbrances or notes secured thereby, which said mortgages attached to the said properties, and that their responsibility for payment of

"said indebtedness" should apply "only to such sums of money as may be by them or either of them received from the sale, hypothecation or rentals of said property, and then only so much thereof as is called for by said encumbrances." It was further resolved that any and all profits which might thereafter accrue from the sale, rental or hypothecation of the property over and above the amount of the mortgage indebtedness should be and remain the sole and exclusive property of the four individuals, "each owning an undivided one-fourth interest therein."

Pursuant to the resolution adopted at the meeting of Arteraft's board of directors on February 1, 1946, the title to the 100 duplexes on Tract 13163 was conveyed to Pool, Murphy and their wives, as tenants in common, by a deed bearing date of March 21, 1946.[1] In the deed, it was stated that the grant therein was "Subject to any and all encumbrances thereon, none of which are in any wise assumed by said grantees or either or any of them."

The total cost to Arteraft of the properties, title to which was so transferred, had been $588,886.81, consisting of $63,013.81 representing land and subdivision costs and $525,873 representing the cost of the buildings. The amount of the F.H.A. insured loans was $724,685 and the excess thereof over Arteraft's cost for the project was $135,798.19. Art-

[1] There is some testimony to the effect that a similar deed covering the said properties was delivered to the four individuals at or about the ti of the said directors' meeting.

craft did not transfer the full amount of such excess to its four stockholders, as called for by the directors' resolution of February 1, 1946, but instead, transferred only $100,464.98 thereof. And, so far as appears, it transferred to the said individuals no amount representing the excess of the rents or payments received in respect of the said properties up to February 1, 1946, over the $20,000 specified by the directors' resolution of April 1, 1945, or the $90,000 specified by the resolution of February 1, 1946.*

The apartment buildings on Tract 11764 and the duplexes on Tracts 11451 and 13163 were, to some extent, of better quality, both in workmanship and materials used, than the houses theretofore built and sold by Arteraft. Pool, for instance, had specified the use of metal lath, instead of plasterboard.

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* It thus appears that the amount representing the excess of the F.H.A. insured loans over the cost to Arteraft of the project, or $135,798.19, exceeded the portion of the loan proceeds distributed by Arteraft to its stockholders, or $100,464.98, by $35,333.21. The stipulation describes an identical amount, $35,333.21, as "additional payment by stockholders to Arteraft." It would accordingly seem that what could have happened was that Arteraft merely retained as its own $35,333.21 of the loan proceeds remaining after paying all of the project's costs and transferring the $100,464.98 to its stockholders. There is some indication from petitioners' proposed findings of fact No. 6 that the $35,333.21, whether it represented an actual payment or merely a retention by Arteraft of a portion of its own borrowings, was in lieu of retention by Arteraft of any part of the rents or payments which had been received by Arteraft in respect of the said properties

The 100 duplexes on Tract 13163 were leased as they were completed, all of the leases being for a period of one year. The dates of completion were in June, July and August of 1945.

From time to time, a tenant would inquire as to whether the housing occupied by him under the lease might be purchased. None of the leases carried a purchase option provision, however, and the tenant was advised that the housing was not for sale. The same response was given to non-tenants making similar inquiries on various occasions.

Effective October 15, 1945, "sales ceilings on all priority assisted housing" were removed, but "OPA controls over rental remained. At some time in 1945 or early 1946, an application was made by Associations and/or Arteraft for permission to increase the rents being charged on the apartments and duplexes, but the application was denied. As to the 170 duplexes, and upon advice of counsel, a practice was later adopted of not renewing leases when they expired, and thereafter a tenant, upon expiration of his lease, would continue in the premises under a month-to-month tenure. The date of the last of the written leases on any of the 100 duplexes on Tract 13163 was April 10, 1946.

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up to February 1, 1946, the proposed finding being that "Arteraft entered into a contract with Associates on February 26, 1945, pursuant to which Arteraft agreed to build 100 duplexes for Associates. It was agreed that Arteraft was to receive $20,000.00 out of rentals as its fee for building. Associates, however, actually paid Arteraft $35,333.21 for building the 100 duplexes." According to Arteraft's 1945 and 1946 returns, it received during those years as rent $54,787.39 and $9,765.44, respectively.

Edward Pool and Associates maintained no office as its own and did not purport to have any employees. Its books and accounts were kept by a Mrs. Woodruff, who was carried as an employee of Artcraft, no part of her salary being charged as such to Associates.

After the transfer of title to the 22 apartment buildings and the 70 duplexes by Artcraft to its stockholders in 1944, and the similar transfer of title to the 100 duplexes in 1946, the rental of the apartments and duplexes was continued from Artcraft's office and in Artcraft's name. In the leases made, Artcraft was shown as the lessor. As received, the rental payments were deposited in Artcraft's bank account by Mrs. Woodruff, who likewise did the bookkeeping for Artcraft. Artcraft would pay the monthly bills, which included utility bills, bills for maintenance, lawnwork, painting and supplies, by checks drawn on its bank account and would charge the amounts so paid on its books to the account of Associates. At the end of the month, Mrs. Woodruff would draw a check on Artcraft's bank account in favor of Edward Pool and Associates covering the net rentals for the month, or possibly the greater part thereof. This check would be signed by either Pool or Murphy, and would then be deposited by Mrs. Woodruff in Associates' bank account. Also monthly, she would draw four checks in equal amounts, one to each associate, on Associates' bank account. She would usually deliver the checks drawn in favor of Pool and Murphy in person, but would send the check in favor of their

wives through the mail. She would not make these checks for the entire balance in the account, but would leave some amounts to accrue, for the payment of "taxes and insurance and things that came due at the end of the year."

A different procedure was followed in the renting of space in the market building and the collecting and handling of the rent thereon. In the leases made, Edward Pool and Associates was shown as the lessor and in keeping therewith the checks for the rent were made payable directly to Edward Pool and Associates, and not to Artcraft. These checks were not deposited in Artcraft's bank account, as was true of the checks covering the rent on the apartments and duplexes, but were deposited directly in the bank account of Edward Pool and Associates. No entries with respect thereto were made on Artcraft's books. Expenditures relating to the market building, such as taxes, were made by checks drawn on Associates' bank account. The handling of the rental checks and the drawing of checks to cover taxes and the like were done by Mrs. Woodruff.

As covering services performed by Artcraft as "rental agent" for Associates, "Associates paid Artcraft the following amounts: 1944, $7,745.88; 1945, $9,357.60; 1946, $23,614.44; 1947, $15,500.00; 1948, $12,000.00; 1949, $12,000.00."[1]

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[1] This finding is according to stipulation of the parties. There is, however, no showing as to how or on what basis the amounts indicated were fixed or paid. The partnership return of income filed by

After the lifting of the ceiling on the sale prices for war housing in October of 1945, and as veterans returned and began looking for homes, a very substantial upward trend, particularly in 1946, became noticeable in the selling prices such housing was commanding.

At some time in January or February of 1946, Philip Boland, who throughout his business life had been engaged in some activity as a real estate broker, was on terminal leave from the Air Force. During that eriod he was visiting "different people" he knew, among them Pool and Murphy, who showed him the properties they had constructed and then owned. Boland, casually but not seriously, because he did not know where he would locate, suggested that Pool and Murphy permit him to sell the properties for them. The proposal was not accepted. At some time in April of 1946, Boland approached Pool and Murphy in a serious effort to induce them to permit him to sell the apartment buildings and the 170 duplexes. He argued that the then present was the best time to cash in on property, that everybody wanted to buy but there was

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Associates for the fiscal year ended January 31, 1945, disclosed claimed deductions of $3,369.89 as Office Expense and $9,368.79 as Commissions, Collection Charges, etc. The return for the fiscal year ended January 31, 1946, disclosed deductions similarly designated, of $9,360 and $387.89. On the returns for the fiscal years ended January 31, 1947, 1948, 1949 and 1950, deductions were claimed under the heading of Office Expense of $25,926.94, $14,000, $12,000 and $12,000, and under the heading of Rental Commissions of $425.70, $558.30, $576.28 and $517.21.

nothing to sell, and that the demand was great for any kind of living quarters. Murphy saw it his way, and it was not until later that Pool "more or less reluctantly" agreed to go ahead and sell some of the units,* the units then agreed upon being 70 duplexes on Tract 11451. For the services, Boland at first sought the "straight five per cent commission" which was "more or less traditional" in that area. After some discussion, an agreement was reached that the petitioners would supply the office facilities, including telephone and some secretarial and office help, and that Boland should be compensated at the rate of $500 for each building sold.

In the course of his negotiations with Pool and Murphy for permission to sell the duplexes, Boland visited the Los Angeles offices of the Bureau of Internal Revenue, and was referred to various rulings and regulations dealing with the sale of the property. He had at one time been an employee of the Bureau. After reading the rulings and regulations, he advised Murphy that in his opinion the gains realized upon the sale of the properties would be capital gains.

On some undisclosed date, but after December 31, 1945, the certified public accountant who looked

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* It was Pool's testimony that Murphy got rather enthusiastic as the prices went up, but that he, Pool, still didn't want to sell them. He also testified, "We got so much advice from Mr. Boland, Mr. Boland was so persistent on what they could do, the prices he could get, and naturally there was quite a profit on them, and they just finally overrode me, that's all."

after the books of Artcraft and of Edward Pool and Associates had undertaken to convince Pool and Murphy that they should sell the duplexes and possibly the apartment buildings. Pointing out that they were restricted in the receipt of rental income by rent control, and stating that in his opinion the prevailing prices for such property were at a peak and would not be as favorable thereafter, he argued that the sales proceeds could be put into more favorable income-producing properties. And while the figures disclosed a rather substantial rental income, he made some tabulations which were designed to show that if depreciation should be computed on the current selling prices for such housing, instead of cost, no profit from rental would be reflected. On or about the first of May, 1946, Murphy inquired as to whether the gains upon sale of the properties would receive capital gains treatment. He was taken by the accountant to his senior in the firm, who advised Murphy that the gains would be taxable as capital gains.

Boland conducted his selling activities in and from the offices maintained under Artcraft's name, and was assisted in the office and paper work by Mrs. Woodruff. He had no sales assistance in selling the 70 duplexes on Tract 11451, but at one time did employ a girl for work in the office. She was compensated by Boland on his own account. Mrs. Woodruff continued to be paid as an employee of Artcraft and received no compensation from Boland. In selling the 70 duplexes, signs were at first placed in front of buildings which had va-

cancies in them. After a short time, this practice was abandoned, to the end that people would then come to the office, from which Boland would send them to the places which were vacant, advising them that if they wanted the property, to come back and "we will do business here."

Boland wrote the copy for and placed and paid for the advertising in the papers of the area. The duplexes were advertised as having been built by Artcraft and as being for sale by the builder. They were advertised for sale at $11,800 per duplex. Representation was made that "rent of one apartment" would carry "payments on the building." There was no offering, and no sales were made, of any of the 70 duplexes on the basis of single living units; in other words, there was only one buyer for each duplex.

The first deposit on a property was taken on May 4, 1946, and in approximately ten weeks' time sales had been closed or deposits had been taken on all 70 of the duplexes. So far as appears, the first closing was on June 22, 1946, and the last on September 6, 1946. The date of closing on one sale is not shown, but the deposit in that instance was made on May 6, and the deed was dated May 28.

After concluding his selling activities in respect of the 70 duplexes on Tract 11451, Boland took a trip back to his home in Missouri. He returned to the Long Beach area about the middle of July, and shortly thereafter, reached an agreement with Pool and Murphy for the sale of the 100 duplexes on Tract 13163, which apparently was in all ma-

terial respects the same as that under which the 70 duplexes had been sold. At or about that time, the selling of such housing was made easier, due to the fact that through so-called GI loans a veteran could borrow the full price of a property and make a cash purchase, without having on his own account to make a down payment.

While in the selling of the 70 duplexes each duplex had been sold to a single purchaser, the advertising of the 100 duplexes suggested two purchasers per building, and most of them were so sold. In so making these sales, it was assumed that the Bank of America would do the financing, as it had done in respect of the 70 duplexes. But when application was made for financing the sale of a duplex to two veterans, each to own one-half of the building, the bank declined and the completion of the sales of the duplexes on Tract 13163 had to be delayed until the necessary financing could be arranged. Murphy set about the job of arranging the financing, and was so occupied for a period of several weeks. He "finally arranged for it in the East," and most of the sales were thereafter financed by the Massachusetts Mutual Life Insurance Company. Deposits were taken on 20 duplexes in August, the first shown as having been made on August 12. The date of the first deed was September 23, six being shown for that date.

As in the case of the 70 duplexes on Tract 11451, the 100 duplexes were advertised as having been built by Arteraft and as being for sale by the

builder. In one instance the representation was, "It's The Builder That's Selling Them!" The price advertised was $13,000 per duplex.

The selling operation was conducted in substantially the same manner as in the case of the 70 duplexes, except that Boland, for part of the time at least, employed two salesmen to assist him. As before, the selling was done from the Artcraft office, and he was assisted in the office and paper work by Mrs. Woodruff. Boland paid the salesmen, but Mrs. Woodruff received her pay as an employee of Artcraft.

The selling of the 100 duplexes extended through the remainder of 1946 and into 1947. The first closing was on October 23, 1946, and by the end of July 1947, 99 of the transactions had been closed, three being closed in the latter month.

Sales of the duplexes would have been facilitated by the existence of vacancies. Due to rent control, however, it was still not possible to have the properties vacated preparatory to sale and in connection with the selling operations the creation of vacancies was encouraged. When the selling of the 70 duplexes on Tract 11451 began, only two units were vacant, but in the course of the selling operations the number increased to thirteen. With respect to the 100 duplexes on Tract 13163, at least 22 units were vacant or became so by the time the sales were concluded. The percentage of tenants who became purchasers was comparatively quite low.

In selling the 70 duplexes on Tract 11451, and

by months, the deposits were taken, escrow was started, deeds were executed and the transactions were closed, as follows:

| 1946 | Deposits Taken | Escrow Started | Deeds Executed | Transactions Closed |
|---|---|---|---|---|
| May | 55 | 11 | 8 | .... |
| June | 8 | 40 | 37 | 19 |
| July | 5 | 12 | 18 | 38 |
| August | .... | 4 | 7 | 10 |
| September | .... | .... | .... | 1 |
| October | .... | 1 | .... | 1 |
| | — | — | — | — |
| | *68 | **68 | 70 | ***69 |

* Two dates of deposit are not shown.

** Two dates escrow started also are not shown.

*** One date of closing is not shown.

In selling 99 of the 100 duplexes on Tract 13163, and by months, the deposits were taken, escrow was started, deeds were executed and the transactions were closed, as follows:

| 1946 | Deposits Taken | Escrow Started | Deeds Executed | Transactions Closed |
|---|---|---|---|---|
| August | 20 | 15 | .... | .... |
| September | 27 | 7 | 13 | .... |
| October | 17 | 25 | 28 | 24 |
| November | 14 | 16 | 20 | 11 |
| December | 5 | 14 | 13 | 17 |
| 1947 | | | | |
| January | 2 | 11 | 13 | 13 |
| February | 1 | 2 | 3 | 18 |
| March | 5 | 1 | 2 | 6 |
| April | 1 | 3 | 2 | 2 |
| May | .... | 2 | 2 | 2 |
| June | 1 | 2 | 3 | 3 |
| July | .... | .... | .... | 3 |
| | — | — | — | — |
| | *93 | **98 | 99 | 99 |

* Six dates of deposit are not shown.

** One date escrow started also is not shown.

The 70 duplexes on Tract 11451 were sold for a total of $828,400, 64 being sold at $11,800 per building and 6 at $12,200 per building. The expenses of sale were $45,316.40 and the depreciation, which had been claimed by Associates in its return of income and, so far as appears, had been allowed by the respondent, was $52,588.94.

The 65 duplexes on Tract 13163 sold by Associates in its fiscal year ended January 31, 1947, were sold for a total of $846,250, 60 being sold at $13,000 per building and 5 at $13,250 per building. The selling costs amounted to $42,447.80. The depreciation claimed by Associates as allowed or allowable on the 65 buildings in its return of income for the said fiscal year was $15,314.26. The 34 duplexes on Tract 13163 sold by Associates in the fiscal year ended January 31, 1948, were sold for a total of $442,750, 31 being sold at $13,000 per building and three at $13,250 per building. The selling costs amounted to $23,753.14, and the allowed or allowable depreciation on the 34 duplexes, as shown by Associates on its return for the fiscal year ended January 31, 1948, was $10,592.01.

On its return of income for the fiscal year ended January 31, 1947, Associates reported gain of $336,947.98 from the sale of the 70 duplexes on Tract 11451 and $413,372.46 from the sale of 65 duplexes on Tract 13163.* It reported a loss of $465.18 on some showcases, and a net gain from the sale of the duplexes of $749,856.26, of which it reported

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* In reporting the gain from the sale of the 100 duplexes on Tract 13163, Associates used $624,-

$374,928.13 as the amount of taxable net long-term capital gain distributable to the partners. On its return of income for its fiscal year ended January 31, 1948, it reported a gain on the sale of 34 duplexes on Tract 13163 of $217,354.06 and a loss on the sale of building fixtures retired of $1,537.60, or a net gain from the sale of the said properties of $215,816.46, of which amount $107,908.23 was shown as the amount of taxable net long-term capital gain.

Each of the four individual petitioners herein reported on their returns for 1947, and as long-term capital gain, one-fourth of the amount which had been reported by Associates on its return of income for its fiscal year ended January 31, 1947, as net taxable long-term capital gain, and on their returns for 1948, one-fourth of the amount similarly shown by Associates on its return of income for the fiscal year ended January 31, 1948.

For the fiscal years ended January 31, 1945, 1946, 1947 and 1948, Associates realized net rentals from the market building, from the apartment buildings on Tract 11674, from the duplexes on Tract 11451, and from the duplexes on Tract 13163, as follows:

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220.02 as its cost of the said duplexes, this amount representing:

| | |
|---|---|
| Land and Subdivision Costs to Artcraft | $ 63,013.81 |
| Building Cost to Artcraft | 525,873.00 |
| "Additional Payment by Stockholders to Artcraft" | 35,331.21 |
| | $624,220.02 |

| Year ended Jan. 31 | Market Building | Tract 11674 22 Multiples | Tract 11451 70 duplexes | Tract 13163 100 duplexes | Total Income |
|---|---|---|---|---|---|
| 1945 | $ 2,235.17 | $ 4,533.55 | $ 9,274.23 | ..... | $16,042.95 |
| 1946 | 15,994.60 | 8,399.10 | 11,356.05 | ..... | 35,749.75 |
| 1947 | 19,567.18 | 6,997.97 | (3,896.13) | $21,597.29 | 44,276.31 |
| 1948 | 16,008.70 | (2,231.51) | ..... | (2,491.07) | 11,386.12 |
| | $53,805.65 | $17,799.11 | $16.744.15 | $19,106.22 | $107,455.13 |

In 1948 Artcraft built for Pool and Murphy on land owned by them individually a business building, referred to as the bank building. This property was sold in 1952 through a real estate broker, purportedly to avoid possible foreclosure. The fee, if any, paid by Pool and Murphy to Artcraft for constructing the building does not appear.

In 1949 arrangements were made with a real estate broker to sell the 22 apartment houses on Tract 11674, and they were sold during the fiscal years 1949 and 1950. Sale of the one remaining duplex on Tract 13163 was completed on February 28, 1949. The gross selling price, cost and net profits from the sales of the 22 apartment buildings were reported by Associates on its returns of income for the fiscal years ended January 31, 1950 and 1951, as follows:

| | | | |
|---|---|---|---|
| Gross sales—fiscal year ended January 31, 1950 | | | $133,938.94 |
| Basis of property sold: | | | |
| Land | $ 12,387.99 | | |
| Buildings | 89,489.49 | | |
| | $101,877.48 | | |
| Less depreciation | 24,459.70 | | |
| | | $ 77,417.78 | |
| Commissions paid Real Estate Agent | | 5,336.29 | |
| Loan prepayment bonus | | 215.00 | |
| Escrow costs | | 917.24 | |
| | | | 83,886.31 |
| Profit from sales | | | $ 50,052.63 |

| | | | |
|---|---|---|---|
| Gross sales—fiscal year ended January 31, 1951 | | | $171,750.00 |
| Basis of property sold: | | | |
| Land | $ 14,454.98 | | |
| Buildings | $122,022.80 | | |
| | $136,477.78 | | |
| Less depreciation | 36,669.58 | | |
| | | $ 99,808.20 | |
| Commissions | | 7,073.30 | |
| Other Charges | | 2,506.51 | |
| | | | $109,388.01 |
| Profit from sales | | | $ 62,361.99 |

In 1950 Pool and Murphy, in association with Major General Patrick Hurley, formed a corporation in New Mexico, the three individuals being the sole stockholders. The business of the corporation was the building and selling of single-family houses, and in 1951 it built and sold 98 such houses. The houses were sold through brokers. Pool was president and Murphy was secretary-treasurer of the corporation, and their duties were the same as their duties had been with Artcraft. Pool and Murphy each received a salary of $500 per week.

In 1951 the three individuals above organized a corporation in Colorado. Its business was the same as that of the New Mexico corporation. At the time of the trial herein, it had built 192 houses for sale and they were in the process of being sold. The positions held with the corporation and the duties performed by Pool and Murphy were the same as those with the New Mexico corporation. From the Colorado corporation, each of them received a salary of $750 per week.

"In the audit of the four individual returns for

1944, the revenue agent proposed deficiencies based on his conclusion that the property comprising Tract 11451 and also Tract 11674 had been transferred by Artcraft to its stockholders at an amount less than the fair market value of the property. The difference between the transfer price and fair market value, the revenue agent concluded, constituted a dividend to the individuals. This issue was settled by agreement that the individuals had received a dividend totaling $30,149.36, of which $20,776.82 applied to Tract 11451 and $9,372.54 applied to Tract 11674. The basis of the property was then increased by the individuals by the amount of the dividend for purposes of determining depreciation and gain from the property when sold." [10]

Artcraft had reported in its return for 1944 a net loss of $44,040.09. In its return for 1946, it applied $23,369.86 as a net operating loss carry-over from 1944 and a further net operating loss carry-over of $8,076.15 from 1945 in arriving at 1946 taxable net income. The respondent in his determination of deficiency determined that Artcraft in 1944 had realized income not reported in the amount of $30,149.36, which he determined had been realized "by transferring property to its stockholders for $30,149.36 less than its alleged fair market value." With such additional income, Artcraft's losses from operations in 1944 would have been $13,911.23, instead of the net losses reported, and would have been absorbed as a carry-back to 1943.

[10] The quoted paragraph is from the stipulation of facts.

He likewise determined a net income of $31,480.86 for 1943, as against $18,759.97 as reported by Artcraft on its 1943 return and $13,314.78 as shown by Artcraft's books. As a result of the adjustments so made, the net loss carry-over to 1946 from 1944 and that from 1945 were disallowed. He did allow, however, net loss carry-backs from 1947 and 1948 of $692.92 and $5,008.71, respectively. Also in his determination of deficiency, he determined that the 100 duplexes on Tract 13163 had been transferred by Artcraft to its four stockholders in 1946 for $100,464.98 less than the fair market value of the said property, and that, by reason of such transfer, Artcraft had realized ordinary income of $100,464.98, which had not been reported.

Without giving effect to the respondent's determination that Artcraft had realized ordinary income of $30,149.36 in 1944 and $100,464.98 in 1946 from transfers of property to its stockholders, Artcraft's income or losses for 1941 through 1946, per its books, were as follows:

| Year | Amount | |
|---|---|---|
| 1941 | $ 11,705.52 | Loss |
| 1942 | 3,190.15 | Net Profits |
| 1943 | 27,275.34 | Net Profits |
| 1944 | *44,060.59 | Loss |
| 1945 | 8,076.15 | Loss |
| 1946 | **36,479.00 | Net Profits |

* This amount is from the stipulation. The $20 difference indicated by reference to the loss reported on th 1944 return is not explained.

** This figure does not show certain minor adjustments which have been made to correctly reflect income per the books, or the amounts distributed to Artcraft's stockholders as dividends on preferred stock, amounts of Federal income tax paid.

Artcraft's net profits for 1946, after payment of dividends on the preferred stock and provision for Federal income tax, as per its books, were $34,781.41.

In his determination of deficiencies against the four individual petitioners for 1946, the respondent determined that the fair market value of the 100 duplexes on Tract 13163 transferred by Artcraft to them exceeded the "total consideration received therefor" by Artcraft by $100,464.98, and that such excess was income to the petitioners, one-fourth, or $25,116.24, to each. For the years 1947 and 1948, the respondent determined that the gain realized on the sale of the 70 duplexes on Tract 11451 and the 100 duplexes on Tract 13163 was ordinary income and not long-term capital gain, as reported by them.

Beginning with the employment of Boland, the four individual petitioners herein began a business of selling real estate, and from April 1946 the 70 duplexes on Tract 11451, and from July 1946 the 100 duplexes on Tract 13163 were held by them primarily for sale to customers in the ordinary course of that business.

## OPINION

As to Artcraft, the respondent has determined, and now argues on brief, that upon the transfer of the 100 duplexes on Tract 13163 to its stockholders in 1946, it realized gain of $100,464.98, his theory, as we understand it, being that the transfer was a sale of the property by Artcraft to its

stockholders for $100,464.98 less than its fair market value; that in an arm's-length transaction Artcraft would have received a price equal to the fair market value of the duplexes, but since the "sale" to the stockholders was not at arm's length, the tax effect was that Artcraft, at least constructively, received market value for the property, thereby realizing gain in the amount determined.

As to the stockholders, the respondent's position is that a sale of property by a corporation to its stockholders at less than fair market value effects the payment of a dividend in an amount equal to the excess of the fair market value over the selling price; that such excess in this instance was $100,464.98, and that Artcraft's four stockholders accordingly received dividend payments of $25,116.24 each.

The petitioners neither admit nor deny the correctness of the respondent's determination as to the fair market value of the 100 duplexes at the time of their transfer. They do take issue with the proposition that gain is realized by a corporation where it sells property to its stockholders at cost, but at less than its fair market value, and accordingly deny that Artcraft realized gain on the transfer of the duplexes to its stockholders, as respondent has determined. They state, on the other hand, that they "have no quarrel with * * * the theory that a bargain transaction between a corporation and its stockholders is a dividend to the stockholders to the extent of corporate earnings or profits," but "Assuming arguendo that there was a bargain

sale by Artcraft to its stockholders" and that the respondent's valuation of the duplexes is correct, it is their position that the amount of the dividend is limited to $34,781.41, or $8,695.35 per stockholder, and that the balance of the excess of the fair market value of the duplexes over the bargain purchase price "first serves to reduce [their] basis in Artcraft stock * * * and the remainder is a long term capital gain," it having been stipulated herein that Artcraft did have net profits of $34,781.41 in 1946, after the payment of dividends on its preferred stock. It is the primary contention of the petitioners, however, that the four stockholders did not acquire the said duplexes by purchase, but that they were built by Artcraft, not for its own account but for the account of the stockholders, that the building was done by Artcraft for the stockholders pursuant to contract and for a fee, and that for the services rendered the stockholders actually paid Artcraft a fee of $35,333.21, which fee was exactly 6 per cent of $588,886.21, the cost of the project, and thus "establishes that Artcraft received a reasonable fee just as if the contract had been with strangers."

In making the above contention, the petitioners make no mention of the fact that it was Artcraft which financed the project, by borrowing the $724,685 on its own account and without personally obligating its stockholders in any manner whatsoever; that though at an early date the stockholders had declared of record that "they were willing to take over title and become the owners" of the 100 du-

plexes, it was specifically prescribed that they were willing to do so only after the duplexes had been fully erected and completed, and that such taking over and becoming owners must further be subject to the specific conditions that they were not personally or individually assuming any liability for the payment of any amount with respect to such taking over of title or becoming the owners, but only that they should account to Artcraft for so much of the rents and proceeds of sale or other hypothecation of the properties as should be required for the liquidation of the encumbrances on the properties and for which Artcraft and the duplexes remained obligated; and, in addition, were to receive, without obligation, and without restrictions with respect thereto, the overplus of the loan proceeds over the land and building costs, and that they did so receive in cash $100,464.98 of such overplus. As to how the proposition that Artcraft was building the duplexes, not as principal, but under contract for the personal account of its stockholders, "just as if the contract had been with strangers," is to be reconciled with the facts just stated, we are not advised.

There is no claim or suggestion of a claim by either party that Artcraft was not at all times a valid and subsisting corporation, and it is patent, we think, that the role of Artcraft was not merely that of building contractor constructing the duplexes for the account of its stockholders for a fee, but rather it was operating for the account of its stockholders in the same manner that the opera-

tions of any business corporation are presumed to be for the benefit of its stockholders, and there was, in truth, no building of the duplexes by Artcraft for the personal account of its stockholders.

It is likewise patent, we think, that the facts offer no support for the respondent's contention that the transfer of title to the said duplexes by Artcraft to its four stockholders was by way of sale and purchase. The one thing which was at all times made clear was that the four stockholders were to acquire title and become the owners of the duplexes by transfer from Artcraft to them pro rata,[11] and without any personal liability or obligation on their part to pay anything whatever therefor. Such being the case, the end result was no different from any transfer or distribution of property by a corporation to its stockholders pro rata and in their status as stockholders. That a corporation derives no taxable gain from the distribution of assets pro rata among its stockholders is well settled. General Utilities & Operating Co. v. Helvering, 296 U. S. 200. See also United States v. Cumberland Public Service Co., 338 U. S. 451, and Burrell Groves, Inc., 16 T. C. 1163. As to Artcraft, the respondent was accordingly in error

[11] Mathematically the transfers lacked a very small fraction of one per cent of being pro rata. The deed was made to the four stockholders "as tenants in common, each owning an undivided one-fourth interest" in the properties, whereas the Class B common stock was held 14,050 shares by the Pools and 13,950 by the Murphys. Each couple owned 2,000 shares of the Class A preferred stock.

in concluding that it had realized a gain upon the transfer of the 100 duplexes to its stockholders. Anent the contention that the four stockholders acquired the duplexes in a bargain purchase, see V. U. Young, 5 T. C. 1251 and 6 T. C. 357, wherein it was held that a bargain sale of property by a corporation to its stockholders does not result in a realization of earnings or profits to the corporation. Eastern Carbon Black Co. v. Brast, 104 F. 2d 460; Choate v. Commissioner, 129 F. 2d 684; and Palace Theatre v. United States, 148 F. 2d 30, cited and relied on by the respondent are not this case.

Our conclusion with respect to the transfer of the 100 duplexes by Artcraft to its stockholders in 1946, is also dispositive of the issue relating to the net loss carry-over from 1944, the basic question being whether the transfer by Artcraft to its stockholders in 1944 of the 22 apartment buildings on Tract 11674 and the 70 duplexes on Tract 11451, which transfers, for the purposes here, were in all respects similar to the transfer of the 100 duplexes in 1946, resulted in a realization of gain to Artcraft. As we understand the parties, they are agreed that Artcraft did have the 1944 net loss carry-over contended for unless it realized gain upon the transfer of the said properties in that year to its stockholders. For the reasons given with respect to the 100 duplexes transferred in 1946, we likewise conclude and hold that Artcraft realized no gain or profit in 1944 upon the transfer of the

22 apartment buildings and the 70 duplexes pro rata to its four stockholders.

Our next question is as to the Artcraft stockholders, and is whether they each received income of $25,116.24 in 1946 as the result of the transfers to them by Artcraft in that year. For the years herein, the nature and character, tax-wise, of corporate distributions in the hands of shareholders are prescribed by section 115 of the Internal Revenue Code of 1939, and in section 115 (a), a dividend is defined as "any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made." And according to Section 115 (b), "every distribution is made out of earnings or profits to the extent thereof." Section 115 (d) relates to distributions which are not dividends and not out of "increase in value of property accrued before March 1, 1913," and provides that any such distribution "shall be applied against and reduce the adjusted basis of the stock * * * and if in excess of such basis, such excess shall be taxable in the same manner as a gain from the sale or exchange of property."

As to the amount of the 1946 distributions by Artcraft, the facts show that the shareholders re-

ceived $100,464.98, or $25,116.24 each, in cash, and the respondent has determined and claims that they similarly received $100,464.98 pro rata, represented by the excess of the fair market value of the duplexes over $624,220.02, the "price" paid therefor. If the accuracy of this latter $100,464.98 should be a prerequisite to the disposition of the issue under consideration, we would, as the record stands, experience considerable difficulty. We are satisfied, as indicated above, that the transaction whereby the duplexes and the $100,464.98 in cash from the F.H.A. insured loan proceeds were transferred by Artcraft to its stockholders was not a sale, but a corporate distribution pro rata. It would thus appear that the amount of the distribution effected by the transfer of the duplexes would be at least equal to the excess of the fair market value of the duplexes over the amount of the encumbrances to which they were subject at the time of the transfer, since the facts show that the stockholders individually were in no way liable for any amount thereon, but had to account only for the rents and proceeds of sale to the extent of the encumbrances. A difficulty is, however, that while the record indicates that the aggregate of the loans made by Artcraft against the property was $724,685, we are not advised as to the dates of these loans, or as to the payments, if any, which had been made thereon by Artcraft up to the time of the transfer. At first blush, the respondent's determination that the excess of the fair market value of the duplexes over the "price" paid to

Artcraft therefor was $100,464.98 might be taken as some indication that the encumbrances to which the properties were subject at the time received by the stockholders was $624,220.02. But it now appears that of that amount, $588,886.81 represented land and subdivision and building costs to Artcraft, while the remaining $35,333.21 is listed by the parties in their stipulation as "additional payment by stockholders to Artcraft," and we have heretofore noted that the latter amount was the exact difference between $135,798.19, the overplus of the loan proceeds over Artcraft's costs, all of which, pursuant to the action of Artcraft's board of directors, was to have been distributed to the stockholders, and the $100,464.98 of such loan proceeds which the stockholders actually did receive. On the other hand, it may well be doubted that the encumbrances against the properties had prior to the transfer to the stockholders been reduced by any substantial amount, if at all, since, according to the stipulation of the parties Artcraft had a deficit of $29,816.35 at December 31, 1944, and had sustained a net loss from operations of $8,076.15 during 1945, and aside from the depreciation allowance the excess of the loan proceeds over cost represented the only apparent fund which might be available to Artcraft for the purpose of reducing the loans, but of which, as noted, $100,464.98 was transferred to the stockholders. Regardless of these differences, however, and though petitioners have alleged in their petitions, and now argue on brief, that there was no sale of the duplexes by Artcraft

to its stockholders since in the construction of the duplexes Artcraft was merely acting as the contractor for the stockholders, for a fee, and under such facts there could have been no corporate-stockholder distribution by Artcraft to its stockholders as the result of the above transfers, they have nevertheless stipulated with the respondent that "the property was transferred to the stockholders for the actual cost to the corporation for the land and improvements plus an additional amount of $35,333.21." And since the petitioners have not contested the respondent's determination that the duplexes had a fair market value of $724,685 at the time of transfer, which is exactly $100,464.98 in excess of "the actual cost to the corporation of the land and improvements plus an additional amount of $35,333.21," there is no basis of record for concluding that the distribution by Artcraft to its stockholders upon the transfer of the duplexes was not at least $100,464.98, as the respondent's determination indicates.

Although Artcraft in 1946 had no accumulated earnings or profits from which a dividend might be paid, within the meaning of section 115 (a)(1) of the Code, it did have, according to the stipulation of the parties and after the payment of dividends on its preferred stock, 1946 net earnings of $34,781.41, which, under section 115 (a)(2), did supply the source from which a dividend in that amount might be distributed in 1946. And, since, as noted, section 115 (b) provides that "every distribution is made out of earnings of profits to

the extent thereof," it follows that Arteraft did pay a dividend to its stockholders in that year of $34,781.41, or $8,695.35 to each stockholder. And this would be true, even if it be said that the transfer did assume the form of a sale and, as in this case, there was no formal declaration of a dividend. Timberlake v. Commissioner, 132 F. 2d 259. It also follows from the above that the distributions in excess of $34,781.41 are, under section 115 (d), to be applied against and reduce the basis to the stockholders of their Arteraft stock to the extent any such basis remained" and the excess is taxable "in the same manner as a gain from the sale or exchange of property." George M. Gross, 23 T.C.576, and Harry Handley Cloutier, 24 T.C.—— (filed September 19, 1955). In amount, the deficiencies are, of course, limited by the amounts as determined by the respondent.

In the last issue, we have the often quite evenly balanced but constantly recurring question as to

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" The parties have stipulated that the cost basis of the Arteraft stock in the hands of the four stockholders was $32,000. They have likewise stipulated that in 1944 Arteraft distributed to the four stockholders in cash $48,052.26, representing the overplus of the F.H.A. insured loans on Tract 11451 over the land and subdivision and building costs thereon. The record also shows that the respondent determined that at the time the apartment buildings on Tract 11674 and the 70 duplexes on Tract 11451 were transferred by Arteraft to the four stockholders in 1944, the fair market value of the apartment buildings and the 70 duplexes exceeded the "price" at which they were transferred by $30,149.36.

whether property which is sold and upon which gain has been realised, was property used in the trade or business of the taxpayer, within the meaning of section 117 (j) of the statute," or was a capital asset, within the meaning of section 117 (a)." And in so many of the cases now being litigated, the question is made no less troublesome and the correctness of the answer thereto is no more or no less certain, whether it be said that it is a question of law, as in Goldberg v. Commissioner, 223 F. 2d 709, primarily or essentially a question of fact, as in Rubino v. Commissioner, 186 F. 2d 304, King v. Commissioner, 186 F. 2d 122, and numer-

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" Sec. 117. Capital Gains and Losses.

(a) Definitions.—As used in this chapter—

(1) Capital Assets.—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer * * * or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business * * *

* * * * *

(j) Gains and Losses From Involuntary Conversion and From the Sale or Exchange of Certain Property Used in the Trade or Business.—

(1) Definition of Property used in the Trade or Business.—For the purposes of this subsection, the term "property used in the trade or business" means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (1), held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not * * * (B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business.

ous other cases, or a mixed question of law and fact, such as was under discussion by the Supreme Court, in Dobson v. Commissioner, 320 U. S. 489, the one thing which does appear certain being that "No rigid rule can be formulated by application of which it can be determined in every case with finality whether property sold by a taxpayer was held primarily for sale to customers in the ordinary course of his trade or business, or whether it was sold as a capital asset" and that, in the end, "each case must stand on its own peculiar facts and circumstances." Victory Housing No. 2, Inc., v. Commissioner, 205 F. 2d 317.

We have examined and considered the evidence and have set out in considerable detail the prevailing evidentiary facts which appear to us to be established thereby, and it is our opinion that those facts require the conclusion that the duplexes on Tracts 11451 and 13163 were held by the petitioners primarily for sale to customers in the ordinary course of their business and that they were sold to customers in the ordinary course of that business.

As to the original purpose for which the duplexes were held, we are satisfied that it was the intent and hope of Pool to hold them for the production of income through the rental thereof, and that it was with reluctance that he agreed to bring the rental venture to an end and place the 170 duplexes on the market. As to Murphy, however, the record is not so clear. Having observed him in the course of his testimony, taking into account the

self-serving character of such testimony and the phrasing of many of the questions to which he responded, we are not persuaded that at any time he had any intent or purpose than to rent or sell the properties, dependent upon which, in the end, should appear to him to be the most fruitful or profitable venture. As to Lottie Pool and Edna Murphy, the record is wholly silent, and aside from any right of the husband to manage the property of the community, it may well be that, in each instance, the purpose and intent of the husband was the purpose and intent of the wife. In any event, however, there can be no question, we think, that the 70 duplexes, for slightly more than two years after distribution by Artcraft, and the 100 duplexes, for some three to six months after distribution, and before being placed on the market, were used in the conduct of a rental business. It is equally clear from the evidence that at some time during the first three months of 1946, and possibly earlier, Murphy began giving attention to the gains and profits to be derived from the sale of the houses, as against their continuation as rental property, and in this he was supported first by the accountant and then by Boland, and to use the words of Pool, "they just finally overrode" him, the result being that in April of 1946, Boland was employed to manage and conduct the sale of the 70 duplexes on Tract 11451, and in July he was similarly employed to conduct the sale of the 100 duplexes on Tract 13163.

We do not understand the petitioners to contend

that after the agreement with Boland the duplexes were not held primarily for sale, but rather, that they were not held primarily for sale to customers in the ordinary course of their trade or business, their reasoning, as we understand it, being that if the selling operations did constitute the conduct of a business, it was not theirs, but Boland's; that, except as to the routine requirements, such as the making of deeds, they had nothing to do with the selling operations, and that they themselves were merely the passive sellers of investment property looking to the reinvestment of the proceeds, with a view to obtaining a better return thereon.

According to the decided cases, the liquidation of property may or may not be the conduct of a trade or business, dependent upon the circumstances and the manner in which the liquidation is accomplished or carried out. Goldberg v. Commissioner, supra; McGah v. Commissioner, 210 F. 2d 769 and 193 F. 2d 662; Home Co., Inc. v. Commissioner, 212 F. 2d 237; Rollingwood Corporation v. Commissioner, 190 F. 2d 263; Curtis Co., 23 T. C. 740, 752; and D. L. Phillips, 24 T. C. 435. And for the same reasons, it does not follow from the fact that the selling was actually done by a real estate broker, rather than by the property owner or owners, that the selling did not constitute a business of the owners or that the sales were not made in the ordinary course thereof. The petitioners themselves, possibly unwittingly, give support to that conclusion. Artcraft, for instance, even though admittedly selling houses in the ordinary course of

its business during 1942, 1943 and possibly in 1944, did all of its selling through brokers. It also appears that Pool followed the same course in his individual operations, prior to the organization of Artcraft. See and compare Gruver v. Commissioner, 142 F. 2d 363; Brown v. Commissioner, 143 F. 2d 470; Welch v. Solomon, 99 F. 2d 41; and Richards v. Commissioner, 81 F. 2d 369, in which case the selling was done by an agent, who was paid a commission, out of which he was to pay for advertising and other selling expenses of himself and his sub-agents. See also James Lewis Caldwell McFaddin, 2 T. C. 395, and Albert Winnick, 21 T. C. 1029, affd. per curiam, 223 F. 2d 266.

Certainly it may not be said that the sales here were passive or casual, as they were characterized in D. L. Phillips, supra. See also Victory Housing No. 2, Inc., v. Commissioner, supra. A very aggressive and active sales compaign was carried on. Advertising of the properties for sale was regularly placed in all of the leading newspapers of the area and in at least three instances Boland was successful in having the properties discussed in a news item appearing in the real estate section of Los Angeles papers. The necessary arrangements were made for the financing of the sales on behalf of the customers. For sale signs were at first placed in front of the duplexes in which there were vacancies, and they were taken down only because Boland found that his selling operations could more conveniently and effectively be accomplished by directing that prospective buyers come to the office.

In short, all of the usual and normal activities which might reasonably be expected in the conduct of an active real estate selling operation were indulged in.

The facts also indicate and establish that the selling operations were not the mere winding up of a business through the sale of properties used therein because the business had proven to be or was no longer profitable, as in McGah v. Commissioner, supra, and Goldberg v. Commissioner, supra. According to the record here, the rental business had been and continued to be a profitable business. Pool had earnestly desired to continue with it. On the other hand, Murphy became convinced that greater profits were to be derived through the marketing of the duplexes. Pool was overridden, gave his consent, and the employment of Boland was the result.

The employment arrangement with Boland and the conduct of the selling operations give further support to the conclusion that the petitioners, with the employment of Boland, had launched and entered upon a real estate selling business. Boland had at first sought employment as an independent broker, which would have permitted him to receive the regularly established commission of five per cent on sales. The petitioners apparently were not agreeable to that arrangement, and it further developed that Boland was without office facilities and did not even have, and could not procure on his own account, a telephone in the area. It was accordingly agreed that the petitioners were to fur-

nish him with the office from which the selling operations could be conducted, including the necessary telephone. He was also to receive office help, and was materially assisted therein by Mrs. Woodruff, any and all expenses therefor being provided by the petitioners. Furthermore, when difficulties were encountered with respect to the financing for the prospective purchasers, in connection with the selling of the 100 duplexes on Tract 13163, Murphy personally took over and worked at the matter until the financing had been arranged. The continuity and regularity of sales seem to us to speak for themselves. All of the facts considered, it would be difficult to imagine a selling operation or business which was more actively conducted and carried on than the one here.

Many cases have been heard and decided which involved the sale of private housing constructed during the war period. There have been points of resemblance in all of them, and in greater or lesser degrees, there have been points of difference. In some of the cases, either by reason of particular facts or the over-all facts, the decision has been that the properties sold were not held primarily for sale by the taxpayers in the ordinary course of their trade or business. In approximately equal numbers, the decisions have been that they were. In Galena Oaks Corporation v. Scofield, 218 F. 2d 217, affirming 116 F. Supp. 333, the facts appear to us to be in all essential respects comparable to the facts in the instant cases. In that case, the United States District Court for the Southern Dis-

trict of Texas concluded and held that the properties sold were held by the taxpayer primarily for sale to customers in the ordinary course of its business, and in that conclusion it was affirmed by the United States Court of Appeals for the Fifth Circuit. In our view, the decisions of the courts therein and the reasons expressed therefor offer the strongest support for our conclusion here.

In the light of the above, we conclude and hold that the duplexes sold during the taxable years here involved from Tracts 11451 and 13163 were not property used by the petitioners in their trade or business, within the meaning of section 117 (j), and as such property is defined in subsection (1) thereof, but were property held by them primarily for sale to customers in the ordinary course of their selling business, within the meaning of section 117 (a), and that the gain realized was not capital gain, as claimed, but ordinary income.

Decisions will be entered under Rule 50.

[Endorsed]: T. C. U. S. Filed March 5, 1956.

The Tax Court of the United States
Washington

Docket No. 36108

EDWARD POOL and LOTTIE POOL,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

## DECISION

Pursuant to the Memorandum Findings of Fact and Opinion of the Court filed March 20, 1956, the parties on July 31, 1956, having filed an agreed computation of the tax involved, it is

Ordered and Decided: That there is a deficiency in income tax for the taxable year 1948 in the amount of $18,651.22.

Entered August 20, 1956.

[Seal] /s/ BOLON B. TURNER,
Judge

Served August 21, 1956. Entered August 21, 1956.

The Tax Court of the United States
Washington

Docket No. 36109

EDWARD POOL, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent,

## DECISION

Pursuant to the Memorandum Findings of Fact and Opinion of the Court filed March 20, 1956, the parties on July 31, 1956, having filed an agreed computation of the tax involved, it is

Ordered and Decided: That there are deficiencies in income tax for the taxable years 1946 and 1947 in the respective amounts of $5,697.02 and $86,828.50.

Entered August 20, 1956.

[Seal] /s/ BOLON B. TURNER,
Judge

Served August 21, 1956. Entered August 21, 1956.

The Tax Court of the United States
Washington

Docket No. 36110

LOTTIE POOL, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent,

## DECISION

Pursuant to the Memorandum Findings of Fact and Opinion of the Court filed March 20, 1956, the parties on July 31, 1956, having filed an agreed computation of the tax involved, it is

Ordered and Decided: That there are deficiencies in income tax for the taxable years 1946 and 1947 in the respective amounts of $5,697.02 and $86,828.50.

Entered August 20, 1956.

[Seal] /s/ BOLON B. TURNER,
Judge

Served August 21, 1956. Entered August 21, 1956.

The Tax Court of the United States
Washington

Docket No. 36111

WILLIAM K. MURPHY, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent,

DECISION

Pursuant to the Memorandum Findings of Fact and Opinion of the Court filed March 20, 1956, the parties on July 31, 1956, having filed an agreed computation of the tax involved, it is

Ordered and Decided: That there are deficiencies in income tax for the taxable years 1946 and 1947 in the respective amounts of $3,410.79 and $98,-401.48.

Entered August 20, 1956.

[Seal] /s/ BOLON B. TURNER,
Judge

Served August 21, 1956. Entered August 21, 1956.

The Tax Court of the United States
Washington

Docket No. 36112

EDNA MURPHY, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent,

DECISION

Pursuant to the Memorandum Findings of Fact and Opinion of the Court filed March 20, 1956, the parties on July 31, 1956, having filed an agreed computation of the tax involved, it is

Ordered and Decided: That there are deficiencies in income tax for the taxable years 1946 and 1947 in the respective amounts of $3,410.79 and $98,401.49.

Entered August 20, 1956.

[Seal] /s/ BOLON B. TURNER,
Judge

Served August 21, 1956. Entered August 21, 1956.

The Tax Court of the United States
Washington

Docket No. 36113

WILLIAM K. MURPHY and EDNA MURPHY,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent,

DECISION

Pursuant to the Memorandum Findings of Fact and Opinion of the Court filed March 20, 1956, the parties on July 31, 1956, having filed an agreed computation of the tax involved, it is

Ordered and Decided: That there is a deficiency in income tax for the year 1948 in the amount of $17,349.60.

Entered August 20, 1956.

[Seal] /s/ BOLON B. TURNER,
Judge

Served August 21, 1956. Entered August 21, 1956.

The Tax Court of the United States

Docket No. 36108

EDWARD POOL and LOTTIE POOL,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

## PETITION FOR REVIEW OF DECISION OF TAX COURT

Come now petitioners Edward Pool and Lottie Pool, and petition for a review of the decision of the Tax Court rendered in the above entitled matter, and allege as follows:

I.

The above entitled proceeding involves the petitioners' income taxes for the year 1948.

The question presented is whether the proceeds from the sale by petitioners of certain apartment buildings and duplexes, admittedly used in their trade or business, were entitled to the capital gain treatment authorized by Sec. 117(j) of the Internal Revenue Code of 1939, or whether such treatment should be denied on the ground that said property was held primarily for sale to customers in the ordinary course of their trade or business.

It was the decision of the Tax Court that the aforesaid apartment buildings and duplexes were

held primarily for sale to customers in the ordinary course of trade or business and the proceeds from the sale thereof resulted in ordinary income.

II.

The review is sought before the United States Circuit Court of Appeals for the Ninth Circuit.

III.

The petitioners at all times herein mentioned have resided and now reside in the County of Los Angeles, State of California, and they filed their income tax return for the year involved with the Collector of Internal Revenue at Los Angeles, California.

The place where the office of said Collector (now Director) of Internal Revenue at Los Angeles is located is within the Circuit Court of the United States Court of Appeals for the Ninth Circuit, and said Court is the court having jurisdiction of a review of the decision of the Tax Court herein under the provisions of Sec. 7482(a), Internal Revenue Code of 1954, and venue under Sec. 7482(b).

The decision of the Tax Court was entered August 20, 1956. The time for filing a Petition for Review will therefore expire November 20, 1956, under Sec. 7483, Internal Revenue Code of 1954.

Wherefore, your petitioners pray that a review be had of the decision of the Tax Court rendered

in the above entitled matter, and that upon such review said decision be reversed.

Respectfully submitted,

/s/ IRVING I. AXELRAD,
Attorney for Petitioners

Of Counsel:
Mitchell, Silberberg & Knupp

Certificate of Service attached.

[Endorsed]: T. C. U. S. Filed November 5, 1956.

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[Title of Tax Court and Cause.]

## NOTICE OF FILING OF PETITION FOR REVIEW

To: John P. Barnes, Chief Counsel, Internal Revenue Service

You are hereby notified that on November 5, 1956, Edward Pool and Lottie Pool, the petitioners herein, filed a Petition for Review of the Decision of the Tax Court heretofore rendered herein. There is delivered to you herewith a copy of the Petition so filed.

Dated: November 5, 1956.

/s/ IRVING I. AXELRAD,
Attorney for Petitioners

Of Counsel:
Mitchell, Silberberg & Knupp

Acknowledgment of Service attached.

[Endorsed]: T. C. U. S. Filed November 9, 1956.

[Title of Tax Court and Cause.]

## DESIGNATION OF CONTENTS OF RECORD ON REVIEW

To: Clerk of the Tax Court of the United States

You will please prepare, transmit and deliver to the Clerk of the United States Court of Appeals for the Ninth Circuit the following documents and records in the above entitled cause in connection with the petition for review heretofore filed by the petitioner:

1. The complete record and all the proceedings and evidence in the action of the Tax Court.

2. Petition for review of decision of Tax Court and affidavit of mailing.

3. This designation of contents of record on review.

Dated: November 12, 1956.

IRVING I. AXELRAD,
Attorney for Petitioners

Of Counsel:
Mitchell, Silbergberg & Knupp

Acknowledgment of Service attached.

[Endorsed]: T. C. U. S. Filed November 14, 1956.

[Title of Tax Court and Causes 36108-13.]

## ORDER ENLARGING TIME

For cause, it is

Ordered: That the time for filing the record on review and docketing the petitions for review in the United States Court of Appeals for the Ninth Circuit is extended to February 3, 1957.

Dated: Washington, D. C., December 4, 1956.

[Seal] /s/ J. E. MURDOCK,
Judge

Entered December 5, 1956.

Served December 5, 1956.

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[Title of Tax Court and Causes 36108-13.]

## CERTIFICATE

I, Howard P. Locke, Clerk of the Tax Court of the United States, do hereby certify that the foregoing documents, 1 to 85, inclusive, constitute and are all of the original papers on file in my office as called for by the "Designation of Contents of Record on Review", including exhibits A-1 thru R-18 attached to the stipulation of facts, but excluding the exhibits admitted in evidence which are separately certified, in the cases before the Tax Court of the United States docketed at the above numbers and in which the petitioners in the Tax Court have initiated appeals as above numbered and entitled, together with a true copy of the docket entries in said Tax Court cases, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of the Tax Court of the United States, at Washington, in the District of Columbia, this 7th day of December, 1956.

[Seal] /s/ HOWARD P. LOCKE,
Clerk, Tax Court of the
United States

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The Tax Court of the United States

Dockets Nos. 36108, et al.

EDWARD POOL and LOTTIE POOL, et al.,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

## TRANSCRIPT OF PROCEEDINGS

Court Room No. 9, United States Post Office and Court House Building, Los Angeles, California. February 27, 1953—3:00 p.m.

(Met pursuant to notice.)

Before: Honorable Bolon B. Turner, Judge.

Appearances: Irving I. Axelrad, 6399 Wilshire Boulevard, Los Angeles, California, appearing for the Petitioners. Donald P. Chehock, (Honorable Charles W. Davis, Chief Counsel, Bureau of Internal Revenue), appearing for the Respondent. [1*]

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* Page numbers appearing at top of page of original Reporter's Transcript of Record.

The Clerk: Docket Nos. 36108 through 36114, Edward Pool and Lottie Pool and associated cases. Will you state your appearances, please.

Mr. Axelrad: Irving I. Axelrad for the Petitioners.

Mr. Chehock: Donald P. Chehock, C-h-e-h-o-c-k, for the Respondent.

The Court: All right. Tell me what the case is about.

Mr. Axelrad: If it please the Court, this case is a substantial one as far as my clients are concerned. As far as the issues are concerned, there are two. The first one goes through all of the individual Petitioners and is the question whether on the disposition of certain real property in the years 1946, 1947 and 1948, the taxpayers, as they reported and are entitled to having the income taxed as a long-term capital gain, or whether it was as the Commissioner contended, ordinary income.

That issue, of course, in turn, depends upon what the facts show in relation to the application of Section 117(a) of the Code, and Section 117(j). Section 117(a), as your Honor knows, provides that assets held for sale in the ordinary course of business are not capital assets when they are of a type which is subject to the allowance for depreciation. Section 117(j), however, provides that property [3] used in a trade or business of a type subject to depreciation may be disposed of at capital gain rates.

The evidence will show that the Petitioner, Art-

craft Corporation, concerning which there is no such issue—there is another issue on it—was organized by the individual Petitioners in the case, and some others, in 1941, to build houses for sale on individual contracts and on tract housing for their own account. In other words, they were in the building business. The evidence will show that those houses were sold through brokers; that the individuals did not engage, the corporation did not engage in the real estate business.

The evidence will show further that the individual Petitioners in this case bought out the stock of certain other people who had stock in Artcraft Corporation in order to secure 100 per cent control so they could utilize Artcraft Corporation, which was an experienced builder, which had know-how as a builder to build for them certain non-usually salable property, but a kind they could use for a long-term investment. In pursuance of this program, they did buy the stockholders out; Artcraft did build 22 apartments in one tract, consisting of two, three and four rental units. Those were completed in 1943; and the evidence will show that they were deeded over to the individual stockholders and that they held them for rent, mostly under [4] leases, until '49 and '50, when they finally disposed of them for reasons that could not have been foreseen when they originally had them built.

In other words, this is a case not like the usual real estate case, like you might say, the usual familiar partnership case, where they take advantage of the Code to receive capital gain where it

was not intended—this is a case of genuine disposition of investment in real property.

The next tract they built was 70 duplexes, roughly, in the same year, and deeded over to the Petitioners as individuals in 1944; and they rented them for over two years, when we finally disposed of them in the bull market after the war, when many veterans returned to California, and there were not enough houses and real estate prices skyrocketed, so they could almost double the initial cost on sale; and yet, if they continued to rent, it was subject to rent control, and turned out to be a rather poor control, and considerably less than what they could have gotten on sale and reinvestment in other properties. The record will show, further, that these individuals did invest that money in other types of investment property, and that they did not go into the real estate business, as such.

Finally, there was a tract of 100 duplexes, which was not completed until 1945. It was deeded to Petitioners in 1946, and they sold that, beginning in the late summer and early fall of 1946—in each [5] case more than six months after they acquired it. In each case their rather substantial holdings in real estate was disposed of through an independent real estate broker.

The Court: What difference does that make as to whether or not it was property that was disposed of through a broker, someone sold it for them, as against——

Mr. Axelrad: Well, first I would answer your

Honor's question by saying that the Ninth Circuit, as I read the decision, seems to believe that maybe the difference between actively being in the real estate business and disposing of your property for yourself. In other words, the cases have said that you may be in the real estate business involuntarily—that is to say, you might start involuntarily, assuming what I have said is the fact, as the evidence will show. And the Commissioner has contended that mere disposition of this many rental units puts you in the business of real estate because you are selling that many; and I say this was just a passive thing, like one might have disposed of a great number of securities on the stock market; if you got a broker and traded in them yourself you might be in the business of real estate.

The Court: If you have something primarily for sale, it wouldn't make any difference whether you got someone else to sell them for you or sell them yourself.

Mr. Axelrad: I think so. [6]

The Court: You could hold them primarily for sale, instead of doing the job yourself, get someone else to sell them.

Mr. Axelrad: Yes, that is absolutely correct. I think you could sell them and be in the business, and conversely, you could get someone else to sell them and be in the business. But it seems to me to be a point to be considered that you did not actively go in the business.

The Court: That might be some evidence——

Mr. Axelrad: I think it is one of the factors that adds up to the balancing of the case——

The Court: It might or might not; but it is not conclusive.

Mr. Axelrad: I agree it is not conclusive. I think, however, it is relevant and material, and as I read the cases, the courts seem to think so.

The Court: All evidence, facts pertaining to the manner and method of doing whatever the business is, or the taxes are, is evidence which would be material and pertinent. They might or they might not, depending on all the picture, be indicative of something. They might not be indicative of whether it would be pertinent and relevant.

Mr. Axelrad: I think what this case boils down to, what the primary issue falls into, really the major part of the case is whether these people, in [7] good faith, bought these properties with an intention of holding them for a long-term investment. If that can be established, then I think it falls as a matter of law that the disposition, just because their holdings were so large, does not place you in the—Section 117(j) is given no meaning in the Code unless you happen to be a very small operation. It says that if you have property used in your business of a type subject to depreciation, you are entitled to liquidate that business or those assets and get a capital gain. For instance, General Motors might have certain tools or dies which they use in their business, and they are subject to depreciation. When they dispose of them they might very well, under the Commissioner's contention

here, get ordinary income, whereas some other business is going to get capital——

The Court: I don't think this is anything such as that. The mere size—just because it is big isn't conclusive. On the other hand, because something is small isn't conclusive.

Mr. Axelrad: I agree with you.

The Court: And you can have a change—you can hold something for investment, and at the same time, then when you change you decide to sell, there can be a change in the manner of holding. The mere fact that it is bought for the purpose of investment doesn't mean that it wasn't held primarily for sale to customers when sold. All of those things [8] are matters which are pertinent and relevant and make up a part of the picture, from which the conclusions are to be drawn. Sometimes you fall in the line of cases that it is a mere liquidation of items that are held not primarily for sale. On the other hand, when you get your picture complete, there are those cases where rather plainly, even though they started out for one purpose, at the time the sale is changed, I mean is made, the holding is changed. So those are all factors which go to make up the complete picture from which we draw our conclusions as to which it is.

Mr. Axelrad: I would like to submit——

The Court: I just mention those because I don't want us to proceed here with any idea that one or another of these things, because it happens to be there, is necessarily conclusive; because it may or may not tip the scale.

Mr. Axelrad: I think that is certainly a proper expression of the law.

The Court: It is always better to go into the trial of these cases having tossed those matters around ahead of time so counsel can be forewarned in the presentation of his case, and not think he is establishing conclusive, something conclusive, when there might be another factor.

Mr. Axelrad: I just want to point out, because I think we may come into this case, ending up, if —I assume now, for the purpose of this legal [9] discussion, that I will be able to establish what I say will be established, and I may be mistaken, but assuming that is so for the moment—we continue to—it seems to me there is a potential conflict between Section 117(a) and 117(j), unless we distinguish it in this way: When your Honor suggested, which is perfectly true, that a person may originally acquire something for investment and then change their purpose and hold it for sale, I suggest that whenever you have property, the subject of which is entitled to depreciation, which was used in your trade or business, and you decide to sell it, which is a prerequisite before 117(j) can apply, you have then changed your manner of handling; one you have decided to sell, you are holding it for sale, and therefore I say that if, as a matter of law, you cannot change your purpose in order merely to liquidate your investment without being taxed at ordinary income rates, Section 117(j) has in effect banned, if not read out of the statute, at least severely limited, and there is this conflict

—in the Tax Court, the latest one, one being Victory Housing. A review decision in the opinion of Judge Murdock made this very point. That case is on appeal to the Tenth Circuit and I think will be heard very soon. I don't know whether you participated in that decision or not. It doesn't appear who the judges were that agreed with the opinion, but I am suggesting that if the dissension stands as a decision, there is a basic conflict between two [10] sections of the Code, that that is a question of law that will have to be ironed out perhaps in a higher court.

The Court: I would imagine that the majority of the court didn't think there was a conflict.

Mr. Axelrad: Whenever you have a majority and a dissenting opinion on a question of law, the majority surely did not agree with that. On the other hands, the majority in one court sometimes is the minority in the next court.

The Court: Of course, sometimes a unanimous decision by the Tax Court is not in accord with the views of part or all of the Court of Appeals.

Mr. Axelrad: That is right. Any way, I don't want to identify my case with a losing one. I only bring that to your Honor's attention because I thing it is the latest decision in the Tax Court on the subject.

The Court: At this time let me inquire as to whether or not there is any problem here with respect to land and buildings when you start applying 117(j). Of course,—of course, land is not normally regarded as depreciable property.

Mr. Axelrad: That is right.

The Court: I think in the Hazard Case, for instance, we made a decision where part was land, with respect to the two categories, part land and part building. So I mention that just in case there is something to be said about that. [11]

Mr. Axelrad: The buildings, of course, were depreciable, and depreciation is allowed. No question raised about it. There are a number of cases in which real estate showed some capital gain allowance under the provisions of 117(j).

The Court: There is some special mention of that in 117(j), isn't there?

Mr. Axelrad: I think (1) in 117(j), I think, includes—I have it right here.

"For the purposes of this subsection, the term 'property used in the trade or business' means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in Section 23(i), held for more than six months, and real property used in the trade or business, held for more than six months——"

So it expressly covers that, as your Honor suggested; which eliminates that factor. There is no question of the six months' holding period for the capital gain. On the 70 duplexes, they were built in 1944 and they were not disposed of, as the stipulation will show, until, oh, the middle of 1946, or just before that.

The 100 duplexes, however, title, we will show, [12] was acquired by the Petitioners in February, although the deed to which we stipulated was not

delivered, or was not dated until March. There was a question of destroyed deed, but that one month is not crucial. The sales started taking place, the first one, August 21, 1946, which was less than six months after the Petitioners got title. However, the escrow was not closed in any of the 100 sales until well after the six months, and I think the cases will support the position that the holder period for capital gain purposes runs from the time which title is actually conveyed to the person that purchases the property, namely at the end of the escrow, except that in some cases where the Commissioner was able to show that the escrow was unduly delayed purely for tax reasons; and I think there is nothing in the case—I don't understand, however, from the 90-day notice, from the pleadings, that there is any six-month holding period involved in this case, because the 90-day notice merely says, "We are recomputing your income on the basis of holdings that you would regard long-term capital gain as ordinary income." Now, if this were short-term capital gain where you get the same return, but not ordinary income — I tried to determine from the Respondent's counsel whether we were going to have this issue, and while we have gotten along very fine on the stipulation, as far as it went, I never could—he always said he wasn't going to divulge anything, and I [13] say I am at a loss to say whether I have any purpose on the holding period—I am only suggesting, as a purely substantive matter, I don't think there is an issue on that matter in this case.

Now, the other issue in this case is whether the corporation, that is Artcraft, received any income in 1944 when it conveyed these 22 apartment buildings and the 70 duplexes to its four stockholders, as in equal shares, they took these as tenants in common and they were equal stockholders.

The Court: Whether the corporation realized income?

Mr. Axelrad: Yes, whether the corporation realized income.

The Court: What would be that transaction?

Mr. Axelrad: Well, the Commissioner's theory——

The Court: I mean, what happened between the stockholders and the corporation?

Mr. Axelrad: The corporation built these 22 apartment units and the 70 duplexes for the Petitioners; built it under a rather informal arrangement, but it all reflected on the minutes——

The Court: Now, whom are you talking about when you say "for the Petitioners"?

Mr. Axelrad: For the individual people, the stockholders, all the Petitioners of the older corporation, or the stockholders of Artcraft, and they [14] held it in equal shares. They made this arrangement with the corporation, reflected on the minutes of the board of directors of the corporation, which are exhibits attached to the stipulation that we will offer; they agreed to convey these buildings when they completed them, and they did do this. But they did it at their own — in other words, Artcraft did not make a profit on this, and

the Commissioner invoked the provisions of the statute which says that when you sell property, or when you convey property to your stockholders for less than its fair market value, it is a dividend in kind, and taxable to the individuals as a dividend.

Then he goes further and he says, on the other side of the fence, while it is a dividend in kind, it really is not a dividend. When we come to the sale by the corporation to the individuals, it was a bargain sale and therefore they had some gain, they call it income, which enlarged their earnings or profits, as though it appeared in '44, and we have no year '44 because there was a net operating loss in '44 which carried over in '46, and eliminated it in '46. Now, the sides are not before the Court in the '44 transaction, because in the audit of the four individual returns, the individual Petitioners signed an 870 and agreed to pay additional deficiency based on the theory they had received a dividend, and they let the statute run on that, so it can be before the Court, although our position [15] is that $30,000.00 paid under mistake of law, there was no dividend to pay, even assuming the fact this was conveyed at less than the fair market value, and even assuming that it was a dividend, because the corporation was a deficit corporation and it had no earnings and profits. And that brings in the General Utility case, which I spoke of on the first day when the calendar was called, and my learned opponent said that I had misstated the issues of the General Utilities case, as your Honor will undoubtedly recall, as an economic declaration

of dividend in kind by a corporation, and the issue was whether that resulted in income to the corporation; and they held that it did not, nor a dividend to the individuals, except to the extent that it determined earnings and profit. If it is dividend from a deficit corporation, it is not taxable to them and not income to the corporation.

The Court: If they were using this corporation to construct buildings for them at no cost insofar as the construction is concerned, other than actual cost, it would be very surprising that their corporation calls itself a deficit corporation.

Mr. Axelrad: As a matter of fact, on the next—you see, I have simplified this a lot for presentation. They thought they were paying the Court the fair fee because they were letting the corporation collect the rental from these units; but before they [16] were all completed, the individual stockholders felt that that rental, that the corporation was collecting, was their compensation, the corporation's compensation for building the units. However, to be consistent about it, if that is what they were really doing, that should be fixed income to the individuals, and they didn't report it that way. That is why I amended the petition to concede that is not fair payment.

The Court: In the situation to what the transaction was, you may well have the question as to whether or not it was an arm's-length transaction, with respect to those units, I presume.

Mr. Axelrad: Well, I think so, but I say we concede to the extent that this was built at cost—

I think the testimony will show they would not have been built, would not have built this at cost, though; that they did it only because the people they were dealing with, the stockholders, they were going to receive this property, and therefore it was in fact a dividend. But there is no requirement that corporation conduct its activities, that it first makes a profit. That is the issue litigated in the utilities case—the disposition of real estate in another corporation, which was a deficit corporation—I mean, they had some earnings and property but not enough to take care of the value of this stock that was being distributed; and in this Court, with only one judge, Judge Opper, it was a reviewed [17] deal, Judge Opper decided in the Fifth Tax Court that the disposition of a dividend in kind, the consideration of a dividend by a deficit corporation does not result in earnings and profits to the corporation, so that the corporation has no income to the extent that it is not a dividend because of the lack of earnings.

We have arrived at a stipulation. It is quite long. I think your Honor will appreciate, from my statement of the case——

The Court: Let's have the government's statement before you start presenting the matter of record.

Opening Statement on Behalf of the Respondent
By Mr. Chehock

Mr. Chehock: May it please the Court, before making an opening statement here, I think it might

be proper at this time to file an answer to the amended petition in the five cases that the Petitioner filed amended petitions in, namely, Docket 36114, 36109, 36110, 36111 and 36112. Copies of these were given to the Petitioners.

The Court: The answer to the amended petition will be received and filed.

Mr. Chehock: In view of the stipulation that [18] is to be filed here, and in view of the Petitioners' counsel's statement, probably it would not be of any particular avail to me to go into detail as to the facts here, and without any thought of doing it, but rather to state the highlights as the Respondent views them, it seems to me that a resume of the facts that are particularly important might be helpful to the Court.

As Petitioners' counsel stated, the Artcraft Corporation was organized in 1941. From the very first the Petitioners Pool and Murphy had a stock interest in this corporation, and the stipulation of facts will show that from June 1943 on, Mr. and Mrs. Murphy and Mr. and Mrs. Pool have been sole stockholders. Murphy and Pool also have been the active head officers of the corporation during all of this period.

Artcraft built some houses for others on contract in which they made some profit, but primarily during these early years their main income was building houses for sale on their own account and selling them. The facts, it is believed, your Honor, will show that for the period from 1942 to 1950, inclusive, the corporation built, and if my mathematics

is incorrect the stipulation will give the exact figure, but I believe this is right, they built some 522 houses, either single or multiple houses, during this period from 1942 to 1950, inclusive. Every one [19] of these 522 have been sold, either by the corporation or by the individual Petitioners, Murphy and Pool. The only building, I believe, erected during this period that has been retained by them since that time is the market building.

In 1942 Artcraft built for sale some 142 houses and sold them. In 1943 they built some 188 houses in two or three tracts and sold them. In 1943 Artcraft also made application for priorities with the National Housing Administration to get materials to build additional 22 structures referred to by Petitioners' counsel as 22 apartments, and 70 duplexes on another tract, 11451. These particular 70 duplexes are a part of the properties here in controversy.

The Artcraft received approval for their applications to build these war housing projects and received title, FHA insured loans and built the 70 duplexes and the 22; and on or about March 3, 1944, transferred these seventy and twenty-two to the four stockholders at the cost to the corporation for the building of these seventy and twenty-two.

At about the same time, or on or about April 1, 1944, the Murphies and Pools, Mr. and Mrs. Pool and Mr. and Mrs. Murphy, formed this joint venture or partnership, whichever you prefer to refer to it as, thereafter known as Edward Pool and Associates, referred to in the stipulation as Asso-

ciates. And thereafter they operated their joint venture on a January 31st fiscal basis.

The Commissioner has in this case disallowed a claimed net loss carry-over from the year 1944 to the year 1946 by virtue of determining here that the fair market value of the 70 and 22 structures turned over in 1944 had a fair market value of $30,149.36, more than the sales price to the individual stockholders in 1944; and consequently have disallowed the claimed net loss carry-over, taking into accounts further adjustments in '45, also.

Then in 1945 we again find the Artcraft Corporation, in which Murphy and Pool are the active head officers, applying for additional priorities to build an additional 100 duplexes, Tract 13163, which are the 100 duplexes here in question, along with the 70 duplexes already mentioned. Here again Artcraft made application for the FHA insured loans and received them, subdivided the property, built the houses, collected the rental until February 1, 1946, as the houses were completed, and rented; and then on or about March 2, 1946, depending on the date of the delivery of the deed, the 100 duplexes were transferred to the four stockholders for $624,222.02, which was approximately $33,000 more than the cost to the corporation for building them.

On these 100 duplexes the Artcraft Corporation obtained aggregate FHA insured loans of $724,685.00 on these properties, and the Commissioner here has determined that the 100 duplexes as transferred, sold, in other words, to the [21] stock-

holders, had a fair market value of the aggregated FHA insured loans of $724,685.00, and that the difference of $100,464.98 constitute earnings of the corporation and dividend income to the stockholders.

About this time of this transfer of the 100 duplexes to the individuals on March 21st or thereabouts, 1946, the Petitioners actively put the 70 duplexes on the market and started advertising and sold them; and about that time, also, they stopped making, I think the evidence will show, written leases on the property. They started actively selling them around April or May of 1946.

And then in around July or August of 1946 they actively put the 100 duplexes on the market, and by January 3, 1947, all 70 of the duplexes had been sold, and 65 of the 100-duplex project had been sold.

The Petitioner's counsel has mentioned the question of the six months' period there, and if the deed was made on March 21, 1946, and delivered at that time, I think the record will show the two agreements were entered into early August, 1946, and the first grant deed, however, bears the date of September 23, 1946, which is six months and two days subsequent to the March 21st date. And consequently, if it is true that the law is that the acquisition date does not begin until the escrow closes, I think the law is, further, that it is retroactive, either to the date of the grant deed or back [22] to the date that it was put in escrow. It may be the law is only back to the grant deed, but should it be back earlier to the time the property was put

in escrow, some of them would be prior—if it is retroactive only to the grant deed, then the matter of whether the deed was delivered on March 21st and first dated, as I said, on September 23rd, which would be six months and two days—there is a question of law at least as to what the situation is on the six-month period. [23]

From February to July of 1947, then all the remaining duplexes of the hundred project, that is 34 of them, were sold, all except one, which, because of financing, as I understand it, was finally disposed of a year or two later. So we have here before the Court, your Honor,—perhaps I should mention there also that while the acquisition of these 70 and 100 by the individuals from the corporation were in bulk, they were sold by individual houses, and so we had 170 separate sales transactions.

We have here before the Court the years 1946, 1947 and 1948. In the year 1946 the total deficiency, if my mathematics are correct, $99,792.40. $48,-714.50 of that is that of the corporation by virtue of the Commissioner's determination that this $100,-000.00 between the fair market value and the selling price, that is, the difference between $724,000.00 and $624,000.00 is earnings of the corporation, that creates their deficiency of $48,714.50 of Artcraft. The remaining amount of the deficiency charged the individuals in 1946 is by virtue of this same income being determined by the Commissioner as dividend income; $100,000.00 to the individuals.

In the year 1947 we have an aggregate tax defi-

ciency of $426,379.26; and in the year 1948, $57,-607.70. In reporting these sales, the petitioners, the Murphys and Pools use the $624,000.00 base—that is, rough figures—and should [24] the Commissioner be correct in its determination regarding the 1946 deficiencies then the Murphys and Pools in turn would be entitled to an adjustment on their basis as reported. I don't know exactly how much difference that would make in the tax result, but probably $70,000.00 or $80,000.00, along in there.

I think the facts as stipulated will show, your Honor, that for the period these particular 70 duplexes and 100 duplexes were rented, for the fiscal year ended January 31, 1945, we have only the 70 duplexes then on Tract 14151. There was a net rental income of $9,274.25.

For the fiscal year ended January 31, 1946, a net rental income of $11,356.05; which was also from the 70 duplexes only.

For the fiscal year ended January 31, 1947, there was a net rental income of $17,711.16; which would be both from the 70 and the 100 duplexes.

Then for the fiscal year ended January 31, 1948, they had a loss from rental of $2,491.07, making a total net from rent for the particular houses here in controversy, of $30,850.37 for all the period held.

As against that, we have net profit from sales for the fiscal year ended January 31, 1947, of $745,-459.48. And for the fiscal year ended January 31, 1948, of $217,354.06, or an aggregate net profit from sales on these particular 170 duplexes of $962,813.54, as against the net rental income of [25] $35,850.37.

Now, it is the respondent's position here, your Honor, that during the interim here in which these 70 duplexes and 100 duplexes were rented, that in the first place, they were different projects and under rental control, and only eligible persons were eligible to rent these particular properties; that if a purpose existed of rental there, that there was a dual purpose to sell; depending on future events, and within the instructions given by the Circuit Court in the Rollingwood Corporation case, that they were primarily held for sale, meaning essentially or substantially the purpose of sale was one of the substantial purposes for holding these 170 duplexes. But irrespective of that, while we say that is the situation, irrespective of that, once the petitioners have made the decision to actively put these 170 on the market, from then on it is the Commissioner's position that they are held primarily for sale, and consequently the profits are profits taxable under Section 22 (a) as ordinary income and not under 117 as long term capital gain.

While we realize that all these cases are decided on their facts, and there are numerous cases to show, on their individual facts, we feel that this case comes squarely under the import of these warehousing project cases, Rollingwood Corporation, Palos Verdes Corporation, the Bildwell, Inc., case and numerous others, all of which I am sure your Honor is [26] acquainted with.

Mr. Axelrad: If I may just—to show where we differ on the law—there are two statements that Mr. Cbehock just stated that I think show the real

difference in our positions. First, while if we did hold it for rental during this period, we had a dual purpose of selling at a good gain, and in the Rollingwood case, it was a different case completely, tax bearing no relation to that at all. In that case the houses were rented with options to buy from the very beginning, and they were purchased within seven or eight months; whereas in this case we find the Associates holding property for as long as seven years, and as the facts unfold it will show conclusively that they never at any time had an intention to sell these when they acquired them, and through most of the years when they held them.

And the second point he makes, that once these were actively put on the market by Associates, then they were placed in the business of selling houses; and I say they never were actively put on the market by Associates. The record will show absolutely the contrary. There was one transaction made by Associates with independent brokers and they stepped away and never lifted another hand.

The Court: What do you mean by that? You mean that they didn't have anything to do with the sale? They made——

Mr. Axelrad: Oh, they owned the property and they [27] got the proceeds, but sold them by independent brokers and paid approximately $75,000.00 for property that was selling like hotcakes. If they had wanted to engage in the business themselves, which would have been a very prime one, of selling real estate, they could have liquidated for about a tenth of what they did, and probably just

as well. They were not in the real estate business.

The Court: Of course, the fact that they happened to be in a seller's market and they didn't have to lift a hand, so to speak, to sell to the buyers, that isn't particularly indicative of anythng. I happen to have a case that I decided that involved that and——

Mr. Axelrad: The Mauldin case?

The Court: Yes.

Mr. Axelrad: Mr. Chehock tried that case and I handled it on appeal.

The Court: That very argument was made rather strenuously in the Mauldin case, the fact that it was a seller's market indicated that there was an absence of holding for sale or being engaged in the selling.

Mr. Axelrad: But, your Honor,——

The Court: Of course, I had to say that that wasn't true.

Mr. Axelrad: I remember the case very well. You held that the party in that case did everything that was [28] necessary to sell those. Namely, he didn't have a broker and he did what was necessary, said he spent no time at all, and you held he had to——

The Court: I don't think the presence or absence of a broker there was particularly indicative.

Mr. Axelrad: The reason I bring that up——

The Court: It didn't have to be, didn't have to be a broker there, because he happened to be sitting there and wasn't doing anything else.

Mr. Axelrad: In this case, if these people had wanted to be in the business of selling houses, they could have done so. But they chose not to be in the business of selling houses.

The Court: Well, we will see what this case holds. I don't think that we will get into a discussion of what is meant by the case turning on them, because there might be a difference of opinion as to what is meant by case turning on. I have never seen any of these cases yet that if I were allowing the term "turning on," that turned on anything other than the whole picture, and the whole picture is made up of all of these varied things, and when you get through, why, the picture points more one way than the other, and sometimes the presence or absence of a broker is a part of the whole cast of the picture. But I think that for the purposes of the statement, why, we are aware of what we think of all these [29] things so that we can move along with the trial here.

Mr. Axelrad: We have a stipulation to offer. It is quite long and quite complete, concerning the differences of opinion that have been expressed here. I would like to offer it, subject to one reservation. This was being typed in the respondent's office when we were notified this morning that we should be ready this afternoon, and I have not yet had time to compare it with the one we agreed on. I assume it is all right, but subject to checking for typographical and other errors—we have looked at it. There is nothing——

The Court: You may file it and if there is any

question after you check it, raise it and clear it up in the course of the trial.

Mr. Axelrad: And there are, annexed to the stipulation, 18 joint exhibits.

The Court: The stipulation will be received and made a part of the record in the case.

Mr. Axelrad: I would like at this time, if I might, your Honor, to ask for clarification on this point of the holding. I read the 90 day notice from one of the cases, and to the best of my knowledge they all say this: "In determining the partnership income distributable to you as above, the following adjustments have been made for the partnership's fiscal year ended January 31, 1947; Net income per partnership return, $38,227.69, add: Ordinary income on [30] the sale of real property reported as capital gain by the individual partners, "$746,389.74."

In other words, in all the discussions of this case, in the 90-day notice and everything that I know about—there was no question of holding period. Now, the dates that Mr. Chehock gave you if there is a controversy about that, we may get into another substantial issue of fact, and I do not feel that it is raised by the notice we have. But if your Honor feels that it is an issue, we have to be prepared to go to trial on that.

The Court: What do you want me to say?

Mr. Axelrad: I want you — is it proper to ask, to rule whether that is an issue on the case raised by the pleadings.

The Court: You drew the pleadings, the petition.

Mr. Axelrad: The petition doesn't say anything about it, and the answer doesn't say anything about it.

The Court: The answer wouldn't if you wouldn't raise it.

Mr. Axelrad: And I wouldn't raise it, because the 90-day notice—he is now asking that the determination be established on different legal grounds; namely, that this property held for sale in the ordinary course of business, "You didn't hold it long enough." I don't wonder——

The Court: Let me ask you this: If it wasn't held [31] primarily for sale in the course of trade or business, then you claim it was a capital asset and sale of capital assets involves short term and long term gains, doesn't it?

Mr. Axelrad: That is right and——

The Court: And that is part of the claim, isn't it?

Mr. Axelrad: No, the Commissioner's claim——

The Court: Part of your claim.

Mr. Axelrad: My claim is a long term capital gain.

The Court: Well, you better show your facts and then argue it.

Mr. Axelrad: As I understand it, we were supposed to disprove the Commissioner's determination, and his determination was that it is ordinary income. The question is, do we also have to show it is not a short term capital gain.

The Court: Well, wherein does that complicate the situation?

Mr. Axelrad: It complicates it if he has got two grounds which he has properly placed before this Court by the 90-day notice, then I must prove first that these people were not in the business of selling these properties in the regular course; and secondly, that they held each of them for at least six months, and I say by the 90-day notice the second issue, as I remember it, was not raised.

The Court: He couldn't have raised it if he says [32] it is ordinary gain.

Mr. Axelrad: He could have said it was short term capital——

The Court: But he said it wasn't.

Mr. Axelrad: That is right.

The Court: Now, I don't see—if I understood what you said and what he said, I don't see wherein there ought to be any difficulty in the matter, other than the mere matter of setting down dates; because as I understood it, unless there is some basis for a difference as to effect of escrow period on the holding, which would be argued as a court of law, I would think that the dates of those would all be a matter of record, and it would be a matter of listing them, and shouldn't be any serious problem about it, other than listing, because there ought not to be any dispute between you as to dates.

Mr. Axelrad: There isn't any dispute as to dates, but we are dealing with a hundred different transactions——

The Court: I understand. The mere fact that it

is a hundred rather than one doesn't change the showing.

Mr. Axelrad: Well, there is the difficulty—Mr. Chehock in his statement, stated that he didn't know for sure what the law was, it could be this or it could be that. Now, I have a little better idea of what I think the law is, but I know that I could be mistaken. The law is, when title passes, when the escrow closes, as I remember the decisions, provisions, [33] there is no intention to unduly delay the escrow for sale or tax reasons—now, if we must disprove—some of the escrows were open as long as a year, and I could get testimony that the reasons they were open for that long was veterans and FHA loans were not approved for technical reasons, requirements that had to be satisfied, such a certificate of honorable discharge, marriage certificates, divorce certificates and all kinds of technical data for reports and so forth.

Now, if those things become relevant, and they are relevant, as I interpret the law, we have a burden of which I feel it is not our responsibility to undertake under the state of the pleadings.

The Court: Well, I think that if there is a question of what sort of capital gain is that, certainly, on the basis of the deficiency notice, and that is where you have to rest it, it surely would be part of your case as to whatever your showing is, because the determination is that it isn't capital gain at all.

Mr. Axelrad: The determination is ordinary income.

The Court: That is right.

Mr. Axelrad: On the issue, whether there is a capital asset——

The Court: Well, it may be, and may not. It may be 117 (j).

Mr. Axelrad: Well, I assume we will have to argue [34] somewhere else what the pleadings are; and I think it is not properly in the case under the pleadings, and I think it is an afterthought based on counsel's feelings that this case isn't as strong as he would like it to be.

Mr. Chehock: I don't think counsel's statement is proper at all. That isn't true. I am trying to present the facts to the Court and let the Court decide it on the merits, and his insinuations as to where he thinks our weakness and strength is is out of place.

The Court: Well, I may say that interestingly enough I had a similar situation in the first docket I ever heard out here; and we had something arise later—I am happy it arises here now. There we still had open the question of whether or not the law sustained on transactions between husband and wife could be reported on a joint return, and the respondent—I mean,—yes, the respondent disallowed the deduction claim. And in the course of trial the petitioner raised, that is, he proved the transaction between the husband and wife, but he didn't show a thing about when the securities were bought for the purpose of determining holding period. Well, it seemed to me that he should have done so. Although, I didn't appreciate in that instance the fact that respondent's counsel at the

time of the trial had not mentioned it, but argued it on brief.

Well, I regarded it as part of the petitioner's case, and [35] since he felt insecure in saying, "Well, I am smart to know that is not a part of my case"; he came in and wanted the opportunity to show it, and I granted him that opportunity, and that was done.

Well, I feel that that is a part of your case, if that is in there. I mean, if there is a situation there, since capital gains do resolve themselves into two types, short term and long term, depending upon the holding period.

Mr. Axelrad: Well, the point of my contention was, your Honor,——

The Court: And now that we know it is there, as a matter of fully presenting the case, why, I would say that that would indicate that it is a matter of concern to the petitioners; petitioners would prove it.

Mr. Axelrad: We will prove it to the best of our ability, your Honor.

The Court: I don't see where there should be any occasion for anything other than sitting down and looking at the records and agreeing to these dates.

Mr. Axelrad: The dates have been agreed.

The Court: Since there are more of them, a little bit more than was present in that case, of showing when the securities were bought, because there was no conditions at all.

Mr. Axelrad: We will certainly go into the

proof. The determination doesn't say this was not capital gain. [36]

The Court: Naturally, it wouldn't say——

Mr. Axelrad: It said ordinary income.

The Court: ——because on that determination there isn't a question of short term or long term about it, just not capital, according to the determination.

All right. You may proceed.

Mr. Chehock: Your Honor, counsel on both sides have agreed that the returns should go in evidence, and it seems to me it would be an appropriate time at this time to put these returns in, and so if they need to be referred to throughout the trial they could be. And if it meets with the approval of the Court, I would like to offer them in evidence at this time.

The Court: Well, that is going to be quite an operation. We will just relax and let you identify them and have them marked, and not be in a hurry.

Mr. Chehock: Respondent offers into evidence as Exhibit S, the taxpayer's copy of the January 31, 1945 Form 1065 return of Edward Pool and Associates.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit S.)

Mr. Chehock: Respondent offers into evidence as Exhibit T the Form 1065 return of Edward Pool and Associates for the year ending January 31, 1946. [37]

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit T.)

Mr. Chehock: Respondent offers into evidence as Exhibit U the Form 1065 return of Edward Pool and Associates for the year ended January 31, 1947.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit U.)

Mr. Chehock: Respondent offers into evidence as Exhibit V the Form 1065 of Edward Pool and Associates for the year ending January 31, 1948.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit V.)

Mr. Chehock: Respondent offers into evidence as Exhibit W the Form 1065 return of Edward Pool and Associates for the year ended January 31, 1949.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit W.)

Mr. Chehock: Respondent offers into evidence as Exhibit X the Form 1065 return of Edward Pool and Associates for the year ended January 31, 1950.

The Court: Be received and so marked. [38]

(The document above referred to was received in evidence and marked Respondent's Exhibit X.)

**Mr. Chehock: Respondent offers into evidence as Exhibit Y the 1941 return of Artcraft Builders, Inc., Form 1120.**

**The Court: Be received and so marked.**

**(The document above referred to was received in evidence and marked Respondent's Exhibit Y.)**

**Mr. Chehock: Respondent offers into evidence as Exhibit Z the 1942 return, Form 1120, of the Artcraft Buil ·rs, Inc.**

**The Court: Be received and so marked.**

**(The document above referred to was received in evidence and marked Respondent's Exhibit Z.)**

**Mr. Chehock: Respondent offers as Exhibit AA the 1943 return of Artcraft Builders, Inc.**

**The Court: Be received and so marked.**

**(The document above referred to was received in evidence and marked Respondent's Exhibit AA.)**

**Mr. Chehock: Respondent offers in evidence as Exhibit BB the 1944 return of Artcraft Builders, Inc.**

**The Court: Be received and so marked.**

**(The document above referred to was received in evidence and marked Respondent's Exhibit BB.)**

**Mr. Chehock: Respondent offers into evidence as** [39] **Exhibit CC the 1945 return of Artcraft Builders, Inc.**

**The Court: Received and so marked.**

(The document above referred to was received in evidence and marked Respondent's Exhibit CC.)

Mr. Chehock: Respondent offers into evidence as Exhibit DD the 1946 return of Arteraft Builders, Inc.

The Court: Received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit DD.)

The Court: Received and so marked.

Exhibit EE the 1947 return of Arteraft Builders, Inc.

The Court: Received and marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit EE.)

Mr. Chehock: Respondent offers into evidence as Exhibit FF the 1948 return of Arteraft Builders, Inc.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit FF.)

Mr. Chehock: Respondent offers into evidence as Exhibit GG the 1943 return of Edna Murphy. I might state here, your Honor, that I do not have the 1943 return of William K. Murphy, but the returns of the two were the same, and I think counsel is willing to so state that the return of the individuals, instead of putting them both in, the return of [40] the individual may be in—they are filed on

community property, and identical returns, and we will put in only one.

Mr. Axelrad: That is agreeable.

The Court: All right. The 1943 return of Edna Murphy will be received and marked as Exhibit GG.

(The document above referred to was received in evidence and marked Respondent's Exhibit GG.)

Mr. Chehock: Respondent offers into evidence as Exhibit HH the 1944 return of William K. Murphy.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit HH.)

Mr. Chehock: Respondent offers in evidence as Exhibit II the 1945 return of William K. Murphy.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit II.)

Mr. Chehock: Respondent offers into evidence as Exhibit JJ the 1946 return of William K. Murphy.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit JJ.)

Mr. Chehock: Respondent offers into evidence the 1947 return of William K. Murphy as Exhibit KK.

The Court: Be received and so marked. [41]

(The document above referred to was re-

ceived in evidence and marked Respondent's Exhibit KK.)

Mr. Chehock: Respondent offers into evidence as Exhibit LL the 1948 joint return of William K. and Edna Murphy.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit LL.)

Mr. Chehock: Respondent offers into evidence as Exhibit MM the 1943 return of Edward Pool.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit MM.)

Mr. Chehock: Respondent offers into evidence as Exhibit NN the 1944 return of Edward Pool.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit NN.)

Mr. Chehock: Respondent offers into evidence Exhibit OO, the 1945 return of Edward Pool.

The Court: Respondent's Exhibit OO received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit OO.)

Mr. Chehock: Respondent offers into evidence the Exhibit PP, the 1946 return of Edward Pool.

The Court: Be received and so marked.

(The document above referred to was re-

ceived in evidence and marked Respondent's Exhibit PP.)

Mr. Chehock: Respondent offers into evidence as Exhibit QQ the 1947 return of Edward Pool.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit QQ.)

Mr. Chehock: Respondent offers into evidence the joint 1948 return of Edward Pool and Lottie Pool as Exhibit RR.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit RR.)

Mr. Chehock: Respondent offers into evidence as Exhibit SS the 1949 joint return of Edward Pool and Lottie Pool.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit SS.)

Mr. Chehock: Respondent offers into evidence as Exhibit TT the joint 1950 return of Edward Pool and Lottie Pool.

The Court: Be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit TT.) [43]

Mr. Chehock: Your Honor, at this time, and with the Court's permission, I would like to ask permission to withdraw Exhibits C-3, D-4, E-5, F-6,

I-9, J-10, K-11, L-12, as well as all the income tax returns just introduced, Exhibits S to TT inclusive, for the purpose of having them photostated and photostats substituted.

The Court: It may be done.

Mr. Axelrad: If your Honor please, on the first exhibits, not the income tax returns, I think we may want to refer to them during the course of the testimony——

Mr. Chehock: I didn't mean now. I mean at the close of the trial.

The Court: Yes, they will be here in the courtroom throughout the trial.

Now, does that cover your preliminary matters, so to speak, so we can get down to the testimony of witnesses?

Mr. Chehock: I think it does, your Honor.

Mr. Axelrad: I believe so.

The Court: I have in mind not sitting past 5:00 o'clock. It is now about 4:30. Do you want to start and get a half an hour in here, or do you think it would be easier to continue without the interruption of the witness?

Mr. Axelrad: It makes no difference to us: whatever suits your Honor. The witness that I will call, I will not be able to finish in a half hour. [44]

The Court: I had that in mind.

Mr. Axelrad: I don't think it will bother me to have that interrupted.

The Court: Well, if it doesn't, we will run until 5:00 o'clock.

Mr. Axelrad: I call as a witness Mr. W. K. Murphy.

Whereupon,

WILLIAM K. MURPHY

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your full name for the record, Mr. Murphy?

The Witness: William K. Murphy.

Direct Examination

Q. (By Mr. Axelrad): You are the petitioner in 36111 and 36113? A. Yes, sir.

Q. What is your age, Mr. Murphy? A. 53.

Q. Where were you born?

A. Springfield, Illinois.

Q. What was your first gainful full time occupation, other than odd school jobs; when you first went into earning a livelihood, what did you do?

A. Office work.

Q. What kind of office work?

A. Clerical work.

Q. For whom? A. Illinois Track System.

Q. What was your next kind of work?

A. It was clerical work, Illinois Central Railroad.

Q. About what period was this?

A. Oh, 1920, I guess; '21.

Q. After that what did you do?

A. I—you don't mind if I think a minute?

Q. No. It was a long time ago. Think about it.

(Testimony of William K. Murphy.)

A. I think I went to work for the State of Illinois after that.

Q. What kind of work did you do for them?

A. Clerical.

Q. What department or what——

A. Well, several departments; no particular thing.

Q. Then what?

A. I worked for the Capital Coal Company.

Q. Office work again?

A. Well, that was office work, and whatever they wanted me to do—my father's company.

Q. Then what?

A. Then I worked in—you want everything I did? [46]

Q. Just answer the question. What were you doing after you got through with your father's coal business? A. Then I worked with Shell Oil.

Q. What did you do?

A. Ran a station in Illinois; tire company and gasoline station downtown.

Q. Then what?

Mr. Chehock: About when was this?

Q. (By Mr. Axelrad): What period was it, roughly? What year are we to now?

A. Oh, that is about '26, something like that.

Q. What did you do after the Shell Oil Company in 1926?

A. Worked for A. L. Kinsey, K-i-n-s-e-y & Sons.

Q. What was A. L. Kinsey's business?

A. Well, they were in the building business.

(Testimony of William K. Murphy.)

Q. What kind of building business?

A. Built houses.

Q. What did you do for them?

A. Well, I done office work and audited the payroll and things like that.

Q. You were a salaried employee?

A. Yes, sir.

Q. Did you do anything else for them?

A. No, sir.

Q. Real estate of any kind? [47]

A. No, sir.

Q. What was your next job?

A. The next job was with the Keystone Copper Company.

Q. What did you do for them?

A. Well, I handled their business on the Exchange. They had a security listed, and I sort of handled it, I guess you would call it. I was employed by them.

Q. You were employed by them to handle this security listed on the Exchange?

A. Yes, sir. Not handling the securities to brokerage houses—I represented the company in getting the surveys and they were going to list the securities, and I handled the work with the engineers, the auditors from the Phelps Dodge Corporation who made the audit; the chief of the mining school at the State of Arizona who done the engineering and the original work.

Q. Any selling involved in that?

A. No, sir.

(Testimony of William K. Murphy.)

Q. What period are we now in; what year?

A. Up to about '32.

Q. What did you do after that? What were you doing between, say, 1932 and 1938, to speed up this a little bit?

A. Well, I wasn't selling anything.

Q. What were you doing?

A. Well, let's see. I was manufacturing—working [48] for a manufacturing company.

Q. In what capacity? A. Vice president.

Q. What were your duties as vice president?

A. Well, handle the sale of the parts and one thing or another like that.

Q. Where was this? A. Los Nietos.

Mr. Chehock: What state?

The Witness: California.

Q. (By Mr. Axelrad): What did you do after that?

A. Well, I went to work for Pacific Construction Finance.

Q. What year?

A. I think it was 1938 and '39.

Q. When did you come to California? You skipped from Illinois to California?

The Court: He was in Arizona.

The Witness: No. The company was in Arizona.

Q. (By Mr. Axelrad): Did you ever live in Arizona? A. No.

Q. Did you ever work there? A. No, sir.

Q. Where did you work, in Illinois and California? A. Yes.

(Testimony of William K. Murphy.)

Q. When did you come to California?

A. Well, I was out here in 1930 for a syndicate in the east, to buy the Lockheed Air Plant out here, but I never worked out here. I came out here to work in 1933, '34.

Q. When you were in Illinois did you have a real estate broker's license? A. No, sir.

Q. Never sold real estate there?

A. No, sir.

Q. What happened when you came to California? Did you apply for a real estate broker's license? A. Never did apply.

Q. You have never had one? A. No, sir.

Q. What did you do for the Pacific Finance and Construction?

A. Well, I outlined plans, you know, rough drafts of sketches of apartment buildings and home layouts.

Q. What was the business of this company?

A. Finance and construction.

Q. And you were in the office making layouts?

A. Yes, sir.

Q. How long did this work continue? [50]

A. Oh, a couple of years.

Q. And then what did you do when you left them?

A. Then Edward—no, formed Artcraft Builders.

Q. You were one of the incorporators?

A. I don't think so.

Q. Who were the stockholders of Artcraft at the time of its formation?

(Testimony of William K. Murphy.)

A. J. S. A. Smith and Mr. Edward Pool; Mr. Cooke—I think his initials are R. T.; and myself, and I think Mrs. Smith and Mrs. Cooke and Mrs. Pool and Mrs. Murphy.

Q. What was Artcraft organized to do? What was its business, and what date are we talking about now?

A. That was in 19—I think 1943. No, it was earlier than that.

Q. The stipulation, I believe, shows it was 1941.

A. 1941. That is correct, April, 1941.

Q. What was the purpose of organizing Artcraft? What was its business?

A. Our business was to build apartment buildings and homes for individuals on contract.

Q. Did you do anything else? Did Artcraft do anything else? A. When? Anytime?

Q. Well, no, when it was first organized, 1941 to 1943, first couple of years of existence. [51]

A. From January 1,—or April 6, when it was organized, 1941, until May or June 1942, that was all it did, was build under contract.

Q. And then what did it do in May 1942?

A. May 1942 it made an application for priority and took an option on some land in Long Beach and filed an application for subdivision and approval of FHA, and built some single family residences for sale.

Q. Your intention in making the subdivision and getting the priorities was to build for sale?

A. That is what we asked for on the priority;

(Testimony of William K. Murphy.)

asked for sales price, which was given us, and we sold them at that price.

Q. What was the significance of asking for a sales price?

A. Well, we wanted to sell them. You had to have a sales price approved by the War Production Board in order to sell them. And there were two spaces. If you wanted to rent them you put down the rent you applied for, which was a maximum of $50.00 a month, and you didn't fill out the sales price.

Q. But on these particular houses which you state are single family dwellings, you applied for a sales price? A. Yes, that is right.

Q. And you were given a sales price? [52]

A. Yes, sir. We built them and sold them for——

Q. Who sold them, the corporation?

A. Well, let's see. There was three or four brokers. I forget who they are, or who they were, frankly.

Q. In other words, the corporation built them and then engaged some brokers to get rid of them?

A. Yes.

Q. What did the corporation do next?

A. The corporation finished the construction of the first tract, which was the latter part of December, I'd say, 1942, and they in the meantime had made application for 187 priorities to cover Tract 12287 and Tract 12288 for single family detached dwellings for sale. We made application for our

(Testimony of William K. Murphy.)

priorities and application for the subdivision approval by the FHA and the War Production Board.

Q. Did you ask for a rental price?

A. No, sir.

Q. Why not?

A. Because we did not want to rent them.

Q. What did you ask for?

A. Asked for a sales price.

Q. Did you get a sales price? A. Yes.

Q. What was the next activity of the corporation?

A. The next activity was building Tract 11674, which [53] consisted of 22 apartment buildings, and 68 apartments, one bedroom apartments.

Q. At about what time did you get these priorities?

A. Well, I think we received them approximately, sometime in August 1943.

Q. At about this time did something occur with respect to stock ownership in Artcraft?

A. A couple of months prior to that, yes, it did.

Q. What occurred?

A. Well, Mr. Cooke and Mr. Smith didn't want to build rental properties. We discussed it with them and they weren't interested in building any rental properties, and Mr. Pool and myself bought their stock.

Q. Did they feel that was a departure from what Artcraft's business had been?

A. Did they feel what was?

Q. Building rental apartments. A. Yes.

(Testimony of William K. Murphy.)

Q. You went and formed a corporation, you bought stock and now you say that the corporation had been building houses for sale.

A. That is right.

Q. Then I gather that your testimony is that about that time you wanted to build to rent and there was a disagreement among the stockholders.

A. That is right.

Q. And Cooke, you say, and Smith, didn't want to do that? A. That is right.

Q. What was the upshot of the disagreement? How was it resolved?

A. Resolved by Pool and myself and our wives purchasing Smith and Cooke's stock.

Q. From that day to this did Arteraft ever build any houses for sale? A. No.

Q. Did you ever build any single family units for any purpose? A. No, sir.

Q. What did it build?

A. Built apartment buildings.

Q. And you say the first was this tract consisting of 22 buildings? A. Yes.

Q. And there, what was the makeup of the units?

A. They were two apartments, three apartments and four apartment flats.

Q. Did you get a priority to build these?

A. Yes, sir.

Q. Who did you get it from?

A. Well, we made application first for subdivision [55] approval of the tracts with the Federal

(Testimony of William K. Murphy.)

Housing Administration, and when they approved the tract for subdivision as a location for the apartments which we were applying for, we filed an application for priorities.

Q. I hand you here a document which is called "Federal Housing Administration Subdivision Information Form."

Will you tell the Court, if you can, what this document is?

A. That is an application to the Federal Housing Administration to approve property that we propose to build apartment buildings on.

Q. And does that refer to the apartments that you have been testifying, concerning the 22 buildings consisting of 68 rental units?

A. It applies to 22 buildings and 68 rental units, yes.

Q. Is there anything on this form in which you had to state, to get approval of your subdivision, whether it was for sale or rent?

Mr. Chehock: I think the instrument speaks for itself on that as the best evidence.

The Witness: Yes. It says on here, "Number of homes to be built immediately to order,—" it says here, "Sixty-eight rental units. For sale, no." "Outline selling and improvement program contemplated: All rentals." [56]

Q. (By Mr. Axelrad): Now, is this your signature on it? A. Yes, sir.

Q. Was that filed with the——

A. Yes, sir.

(Testimony of William K. Murphy.)

Q. Was it approved? A. Yes, sir.

Q. Could you have gotten the approval of the War Production Board for priorities without this approval of this subdivision?

Mr. Chehock: I object. That calls for a conclusion of law that this witness is not competent to testify to.

Mr. Axelrad: If your Honor please, it will appear more and more that the witness is a man who has a great deal of experience with these administrative procedures, and I want to ask not what the law is, but what his experience is.

The Court: He could tell what he thought it was.

Q. (By Mr. Axelrad): What did you think you had to do in order to get a priority?

A. The procedure, you had to go first and file a subdivision information form for approval of the subdivision.

Q. That is this document?

A. That is right. You have to do that to show the drainage is proper and the location of the land that you are applying for is located close to houses or plants where the [57] war workers would be employed. That was the first step.

When your letter of subdivision approval came out from the Federal Housing Administration, you filed an application with the Federal Housing Administration, which was forwarded to the War Production Board asking for priorities on the number of rental units that you contemplated building, and in the application for priorities you stated if you

(Testimony of William K. Murphy.)

were going to rent them, the amount of rent, shelter rent charged tenant, or that you proposed to charge the tenant; also, the amount of charges for upkeep of the property to each tenant. And you also stated on that if you were going to sell them, you applied for sales price; and if you were not going to sell them, you applied for rental approval.

Mr. Axelrad: If I might inquire at this time, there is a great deal of law relating to war time procedures concerning Federal Housing Administration and War Production, and I assume that the Court will take judicial notice of the administrative procedures insofar as is expressed in regulations in the federal statutes on the subject.

The Court: I may say, that regulations of law—and, of course, regulations, if they are reasonable, have force and effect of law, and naturally, those things may be argued by reference and citations. Now, it is a fact that it could be some of these things might not be too easy to come by. Any easing of that burden, of course, would be helpful. [58]

Mr. Axelrad: On that, the WPB priorities, war production priorities which Arteraft built houses in question here, we have attached to the stipulation as a joint exhibit, various regulations that were incorporated therein by reference; and since we have entered into the agreement of that stipulation, I have found additional amendments which I will introduce as Petitioner's exhibits at a time when we come to discuss it in the testimony. But this requirement of subdivision information form, I think,

(Testimony of William K. Murphy.)

Mr. Murphy's testimony, together with the form itself, will indicate what the parent practice was.

I would like to introduce as Petitioner's Exhibit No. 19 this Federal Housing Administration Subdivision Form relating to the 22 apartments.

The Court: Any objection?

Mr. Chehock: No objection.

The Court: Be received and marked as Petitioner's next exhibit.

The Clerk: No. 19.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 19.)

Mr. Axelrad: I might say, your Honor, that I have been working with the facts of this case—these tract numbers involved here are very confusing, because they are long, and I will refer to these tracts as the 22 apartment and 70 duplex and 100 duplex rather than by the tract number. [59] I think it will make for some clarification to refer to it by number of unit rather than by tract number.

Q. (By Mr. Axelrad): I hand you here a document entitled "Subdivision Information Form of the Federal Housing Administration." Can you explain what that relates to?

A. That is an application for 140 rental units—an application for the approval of the land on which we proposed to build them.

Q. Is that the tract of the 70 duplexes which you ultimately built? A. Yes.

(Testimony of William K. Murphy.)

Q. Was it set on the form with respect to whether this was for sale or——

A. "Sales on outline selling and improvement program: None."

"Number of homes to be built immediately to order: 140 rental units; rentals, $50.00 per month."

"Number for sale: No."

Q. Is that filled out in your handwriting?

A. Yes, sir.

Q. What is that, the office copy? A. Yes.

Q. Was a duly executed copy of that filed with the proper authorities? [60]

A. Yes, with the Federal Housing Administration.

Mr. Axelrad: I would like to offer this as Petitioners' Exhibit No. 20, the Federal Housing Administration Subdivision Information Form concerning the 70 duplexes.

Mr. Chehock: No objection.

The Court: Be received and marked as Exhibit 20.

(The document above referred to was received in evidence and marked Petitioners' Exhibit No. 20.)

Q. (By Mr. Axelrad: Now, you say that before you built the 70 and 22—that is, Artcraft did—Artcraft had been building single family units for sale?

A. Yes, sir.

Q. Why did they build single family units, for instance, rather than apartments or duplexes such as the corporation was now building?

(Testimony of William K. Murphy.)

A. We built single family dwellings because all they had to get down was a hundred or $50.00 down, and had three years, 36 months to pay the balance of the down payment—easier to sell.

Q. They were easier to sell? A. Yes.

Q. Do you know whether anybody was building apartments and duplexes, a speculative builder or for resale?

A. No, I don't know anyone that was. [61]

Q. Were you acquainted generally with the kind of business that was being done? A. Yes.

Q. Why did you and Pool decide to have Artcraft build rental units, as you testified you did, rather than keep on with the business that they had been doing?

A. Well, Mr. Pool and I had numerous discussions. I had a wife and two children at the time, and he had been in the building business for approximately, I think, roughly, 30 years at that time, and he said that, "You are up one day and down the next in the building business, and you can lose a fortune on one deal." And he thought we should have some property for investment, some income that we could rely upon in our old age, and he said more so than I should have it even than he.

Q. Why more so with you?

A. Well, I had a couple of children, and he was the godfather to both of them, and I guess he had quite an interest in them.

Q. What was the reaction of Cooke and Smith to that?

(Testimony of William K. Murphy.)

A. Well, Cooke and Smith wouldn't build any for income at all. We bought them out; that is, bought out their stock, I mean.

Q. Weren't they interested in investment?

A. I don't know. They said they didn't want to build [62] any income property.

Q. Why didn't you build the same kind of houses that you knew how to build, that Artcraft had been building, individual units? Why didn't you hold those for rental?

A. Well, they are not as good an investment as apartment buildings.

Q. Why not?

A. Well, you can get four flats on the same size lot as you can get a single family house on. You get four apartments on there. It cuts the cost of the lots, streets, sidewalks, gutters, sewers and water upkeep, maintenance and everything else. It is four times as much for a single house, approximately, for rental.

Q. In other words, apartments or multiple dwellings here were better long term investment than single family units?

A. That is the standard of any development for investment, would be multiple dwellings. I don't know of any investment ever made in single family dwellings.

Q. That is, by a——

A. By an owner. I am not referring to banks or financial institutions.

(Testimony of William K. Murphy.)

Q. In other words, you say that single family units don't lend themselves to rental investment?

A. That is absolutely correct.

Q. But duplexes and multiple dwellings do? [63]

A. Yes, sir.

Q. What about the converse of it? What about the salability, if you wanted to build for sale, would you build apartments and duplexes?

A. Well, if I wanted to build for sale, I wouldn't, no.

The Court: You wouldn't what?

The Witness: I wouldn't build single family apartments.

The Court: Why not?

The Witness: Because there is no market for them.

The Court: Why not? What was the difficulty?

The Witness: Well, I imagine the down payment was one of them.

The Court: Required more money?

The Witness: That is right. We could only get a one to two hundred dollars down as a down payment on a $3900.00 to $4400.00 house. And in our War Production Board application that we applied for, we specifically stated in there that we did not want to sell them, and I think there is a penalty in there of two years in prison and $10,000.00 fine if we did sell.

Q. (By Mr. Axelrad): Let me ask you, could you have gotten a priority, in your opinion, to build single family units for rental had you desired to?

(Testimony of William K. Murphy.)

A. Yes, sir. Absolutely.

Mr. Chehock: I object to that as going beyond the knowledge of this witness and purely——

The Court: He says his opinion.

Mr. Axelrad: As a matter of fact, we will show by other witnesses that Mr. Murphy was very well acquainted with all of the regulations, as a——

The Court: I don't think we need to argue those things. I think that those things can be proved without relying on opinion testimony; I imagine.

Q. (By Mr. Axelrad): Well, let me ask you, Mr. Murphy: Do you know whether anybody in that general area was building, on war priorities, single family units? A. Yes.

Mr. Chehock: I object to that as being immaterial.

Mr. Axelrad: It is extremely material. Mr. Chehock said in his opening statement that this is another war production real estate case. This case is quite different than any reported case dealing with real estate operations at that time. I think a vital part of our case is to show exactly why this is quite different than any of the other cases. We are bearing the burden of proving that it would not have been possible to build single family units, because the fact is otherwise, and Mr. Murphy is willing to and able to [65] testify——

The Court: Read the last question and answer.

(Record read.)

The Court: Let the record show that I let the question and answer stand.

(Testimony of William K. Murphy.)

Q. (By Mr. Axelrad): I would like to ask you one further question, Mr. Murphy. Were, to your knowledge, single family units built on war production priorities in that general area during the time you were building and holding the 22 and 70 multiple dwellings——

A. Some 2000 were being built at that time.

The Court: We will suspend now until Monday morning.

(Whereupon, at 5:00 o'clock, p.m., an adjournment was taken until 10:00 o'clock, a.m., Monday, March 2, 1953.) [66]

The Court: We will resume the trial in the group of cases on which we started Friday.

Whereupon,

WILLIAM K. MURPHY

called as a witness for and on behalf of the Petitioners, having been previously duly sworn, resumed the stand and testified further as follows:

Direct Examination—(Continued)

Q. (By Mr. Axelrad): You stated on Friday, Mr. Murphy, that you and Mr. Pool purchased all of the stock of Arteraft Builders Inc. as a result of a disagreement with Mr. Smith and Mr. Cooke over what kind of property the corporation should build; is that correct? A. Yes, sir.

Q. When did you first start discussing different types of ideas with the corporation

A. Approximately September 1942.

Q. What proposal was made then and by whom?

(Testimony of William K. Murphy.)

A. Well, at several meetings we held, Mr. Pool and Mr. Smith and Mr. Cooke and myself, we were discussing building rental properties for an investment, and the four of us discussed it, and it was along in the fall, the first discussions, as I remember it, the fall of 1942. We were [69] building the first tract for sale at that time.

Q. Where did those discussions occur?

A. They occurred down on the tract which is in Long Beach, and our office at 1600 South Western in Los Angeles.

Q. I hand you a paper which is entitled "Artcraft Builders, Inc., Meeting of Directors," dated August 18, 1942. Will you read the last two paragraphs?

A. "Mr. Murphy also stated that he had 186 houses with plans to put before the meeting of the directors. Mr. R. T. Cooke suggested that 186 houses at this time was quite a number to finance and suggested that we considered 86 at this time with the balance to be built later. Mr. Murphy was authorized to proceed on this basis, providing same could be financed under our present financial status.

"Mr. Edward Pool also brought up the question of building 27 income units in addition, but this proposal was turned down."

Q. You were present at that board meeting?

A. Yes.

Q. Was there a discussion concerning this?

A. There was quite a lengthy discussion; yes, sir.

(Testimony of William K. Murphy.)

Q. What was the nature of the discussion? In other words, can you explain in any more detail?

A. Well, Mr. Pool and myself wanted to build—discussed with Mr. Cooke and Mr. Smith the fact that we would like to build some investment properties so that we would have an income.

Mr. Chehock: May I ask, counsel, if you don't mind, whether or not you are offering that in evidence and whether or not you have the minute book here to let me compare it.

Mr. Axelrad: I would like to offer this in evidence as an exhibit. This statement that Mr. Murphy read from is from the copy book. There was an original and then there was a copy of all of the minutes, and the original for this period has not been found. It was present when this investigation started. So many people have looked at it, we just can't locate it.

Mr. Murphy, I believe, will testify that this is an exact copy, as far as he can remember, of the original.

Mr. Chehock: I move to strike this testimony on the ground that if it was a part of the original minutes of the meeting, that they would be in a part of the original minute book and not just an unsigned copy. [71]

Mr. Axelrad: This is a conformed copy of the original. I think we will have to bring that out by testimony. The original book went to the revenue agent when the investigation was first started.

The Court: Well, the record shows the situation

(Testimony of William K. Murphy.)

here as it stands now, and we will let it stand subject to the matter being tied up, with the understanding that counsel for the Petitioners will produce for the examination by counsel for the Respondent of whatever it is that he has, with a view to satisfying him and, if need be, the Court that it is authentic.

Now, at this stage I shall observe that we hope that we don't have any more situations like this arise, and if there are other situations of this kind, I suggest that counsel at the first opportunity, intermission or otherwise, bring those matters to the attention of counsel for the Respondent so that they may be cleared in advance of their presentation in the course of the hearing. That is, this is the type of thing that should have been cleared before trial started, under our rule with respect to stipulations, to the end that matters that are authentic may be agreed upon, and those that there is some question about can, if need be, be brought to the attention of the Court.

I am not going to grant the motion to strike at this time, but I will entertain a motion if counsel for the [72] Petitioners is unable to clear the matter with counsel for the Respondent between now and the end of the trial, and then, of course, I will hear what is said and make my ruling.

Mr. Axelrad: May I offer this as an exhibit now?

The Court: No. I would say that you better hold

(Testimony of William K. Murphy.)

it. Let's don't go any further than we have until we get the matter cleared up.

Mr. Axelrad: Now, in this connection, your Honor, there is one more in exactly the same status as this one. That is to say, it purports to be the minutes of the board of directors at a later date, also from the copybook. You see, the situation was this: There were two books kept, as I am informed. One was the original, a signed copy, and then a copybook, and from 1941 to 1943 they had one book and it became filled up and they started a second book. We have the second book which covers most of the matter we are concerned with, but we do not have the original of the first book.

If I may ask to have the witness read from this, subject to the same qualifications——

The Court: Well, I don't want to throw your examination out of order, as you have it planned unduly, but it seems to me that since the matter has been raised here, that we might as well wait until you make your effort to clear this matter. [73]

Mr. Axelrad: Well, I don't know what effort we can make, your Honor.

The Court: I don't know, either, but you haven't made any up to now.

Mr. Axelrad: This man can testify that the original has been lost, and under the best evidence rule, this is permitted. Mr. Chehock is very difficult to satisfy. I have been with him for three weeks on this case and we have done——

The Court: I am not going to read it, but I will

(Testimony of William K. Murphy.)

refer you to our Rules, 31 (b), and it covers just this sort of thing, and under that the normal thing to be expected would be that these matters would have been presented and then if Mr. Chehock remained difficult to satisfy, then instead of just proceeding here in this manner, the matter could be called to the attention of the Court and the Court could be advised as to these things rather than going along and allowing the reading and then having a motion to strike and the matter drawn out with it in the record, but with it in there with some question about it.

Now, if Mr. Chehock is unduly unreasonable and hard to satisfy, why, we can take care of those things if the effort is made and it is brought to my attention so that I can do it, but I think we take up time and we get matter that ought to be together in the record scattered around.

Mr. Axelrad: May I make this inquiry or suggestion? I have here a number of exhibits which are pertinent to Mr. Murphy's testimony. Some of them are carbon copies of letters from their files, which I brought to Mr. Chehock's attention in a very general sort of way. I asked him if he was going to raise any question as to their authenticity. He looked at a couple of them and said no. I thought this was in the same category. I want to make it clear that I did not bring this to his attention.

The Court: We will take an intermission until you bring that to his attention and you gentlemen

(Testimony of William K. Murphy.)

screen them, and then we will see what we have left.

(Short recess taken.)

The Court: On the record.

Mr. Chehock: Your Honor, while Petitioners' counsel has made some pretty harsh statements about me, I would like to say that in my negotiations here the last several weeks in trying to work this stipulation out, that Mr. Axelrad and Mr. Murphy and Mr. Pool have been very cooperative. We have had a few differences, but I believe we have stipulated to quite a few facts.

Now, in regard to this particular problem on these purported minutes here, upon Mr. Axelrad's statement to the Court that these are copies found in the book that he has, I will agree that they are copies found in the book that he [75] has. I will not agree that they are original minutes. If he can prove that the originals have been lost, perhaps this is the best evidence, but I don't know. I can't agree that they are original minutes at this time. But I will agree that if he produces the book that he has that this is a copy of what that book would show.

The Court: Where is the book?

Mr. Axelrad: The book is in my office, your Honor. I will produce the book, but as I understood Mr. Chehock, he will be willing to stipulate on my statement that it came from that book.

The Court: Well, do you want to go ahead here now? What is your view as to the best way to get at them since you haven't seen the book?

(Testimony of William K. Murphy.)

Mr. Chehock: My statement is, your Honor, that if he does produce the book which does purport to be a copy of the original minutes, that I will agree that the copy of the original minutes as they produce them is identical with what they produce here. I will not agree that these constitute original minutes.

The Court: Which one of these is it that you read from?

Mr. Axelrad: This one (indicating).

The Court: All right. Let that be marked for identification as the next exhibit. [76]

The Clerk: It will be Petitioners' Exhibit 21.

(The document above referred to was marked Petitioners' Exhibit No. 21 for identification.)

The Court: Now, let's go ahead at this time, since we are on these things, and you can present whatever you have to offer by way of testimony or otherwise which would indicate, according to your views, that this is the best evidence.

Mr. Axelrad: Speaking only of this one?

The Court: Well, speaking of that one, too, as far as that is concerned. I think you can proceed on this one that has been marked for identification and possibly you would have the same pattern on both of them.

Mr. Axelrad: Right.

Q. (By Mr. Axelrad): What was your capacity, what position did you hold in the corporation at the period we have been speaking about, 1942 and 1943?

(Testimony of William K. Murphy.)

A. Well, in 1942 I was in charge of the sales. In 1943, in part of 1943, I was, I think, director and secretary and treasurer.

The Court: Now, you weren't secretary, apparently, when this meeting was supposed to have occurred. It is signed by Cooke as secretary.

The Witness: Yes, sir, that is correct. [77]

Q. (By Mr. Axelrad): You became secretary at a later date, after Mr. Cooke and Mr. Smith were bought out? A. Yes, sir.

The Court: Where is Cooke?

Q. (By Mr. Axelrad): Is Cooke available?

A. I don't know. We could find out.

Q. What about Smith?

A. He lives here; yes, sir.

The Court: What official position, if any, did Smith have?

The Witness: When those minutes were signed, Mr. Smith was president and Mr. Cooke was——

The Court: Secretary?

The Witness: I think he was secretary and treasurer; yes, sir.

The Court: Well, you may proceed with the other to have it marked for identification, and that is the minutes for what time?

Mr. Axelrad: The minutes of Arteraft Builders, Inc., minutes of the directors at a special meeting held on February 17, 1943.

The Court: All right. That will be marked as the next exhibit for identification [78]

(Testimony of William K. Murphy.)

The Clerk: This one is Petitioners' Exhibit No. 22 for identification.

(The document above referred to was marked Petitioner's Exhibit No. 22 for identification.)

The Court: Now, I think that in that situation it will be better just to allow it to stand for what it is and not have excerpts read from it into the record at the present time, because if we do and we find later we are not justified in having it in, we will have to strike it.

Q. (By Mr. Axelrad): How many minute books did the corporation keep, if you know?

A. Well, they kept one original minute book, but we ran out after a year and a half or two years, and we had to get a new one.

Q. You mean a new physical cover so that you had two volumes; is that right? A. Yes, sir.

Q. Did you have any copies of these?

A. We had a copy of each one; yes, sir.

Q. In other words, there were two books—there were four books, two originals and two carbons.

A. Yes.

Q. Have you ever seen them all together at one time? A. Yes, sir. [79]

Q. When was the last time you saw them all together?

A. Well, to the best of my recollection it was along in the latter part of 1949.

Q. Where were the books then?

A. They were in my possession.

Q. Where?

(Testimony of William K. Murphy.)

A. At my office. I delivered them——

Q. Who did you deliver them to?

A. I delivered them to Mr. Erwin Lampe of Arthur Young & Company.

Q. And what was his relationship to you or Artcraft?

A. Their firm was our auditors and tax counselors.

Q. What did you deliver them to him for?

A. He told me that the Internal Revenue agent wanted to see the minutes of Artcraft Builders, Inc., and I told him—I asked him, did he want the copies of the originals, and he told me to bring both the originals and the copies, so I took the two books that contained the original minutes and the two books that contained the copies down to Mr. Lampe's office of Arthur Young & Company and left them, and I have never seen them since.

Q. You haven't seen any of them since?

A. I saw them over there Saturday in your office.

Q. What did you see in my office Saturday?

A. The second volume of the minutes, the second [80] volume of the original minutes and both volumes of the copies, the first and second.

Q. The copies of the first and second?

A. Yes.

Mr. Axelrad: May I say something off the record?

The Court: Let it be off the record.

(Discussion off the record.)

(Testimony of William K. Murphy.)

The Court: On the record.

Q. (By Mr. Axelrad): Mr. Murphy, you testified concerning this disagreement between you and Mr. Pool and Mr. Smith and Mr. Cooke. Was this just a routine disagreement or did something occur that fixes it in your memory?

A. Well, I don't know what you mean by a routine disagreement.

Q. Well, was this a casual thing or were there heated discussions about it?

A. No, it was a heated discussion upon several instances. Mr. Pool, as an officer of the corporation, was, I would say, more in the midst of it than I was. However, I was present upon numerous occasions when these discussions were held, and Mr. Smith was very insistent that no income property be built, or property for investment, and Mr. Cooke agreed with him. And upon one instance I remember Mr. Pool stating that he wanted the record to show [81] that he wanted income property.

Q. Did these discussions occur in official meetings of the corporation?

A. Two of them did that I remember, and then there were several I would say informal discussions. That is, we weren't having a board meeting at the time.

Q. Why was it, if you and Mr. Pool wanted to build income property for an investment, as you have testified, that Arteraft ended up building them?

A. Well, the contractor's license was in the

(Testimony of William K. Murphy.)

name of Arteraft Builders, Inc. They had the wherewithal, the equipment and the necessary personnel. They had all th compensation insurance. They had the credit, and all your old age pension setups, and in addition to that, there would be no liability on our part. They had the public liability and property damage insurance.

Q. It is your testimony, then, that Arteraft was chosen to build it because it was in a position to build? A. Yes, sir.

Q. And then the plan was to deed the property to you as individuals?

A. Well, the plan, we proposed to purchase the property from Arteraft on the first tract of 22 buildings, apartment buildings, prior to the time the land was ever purchased and—— [82]

The Court: Maybe you better state that again. That is a little bit involved.

The Witness: We proposed——

The Court: Who proposed?

The Witness: Mr. Pool and myself and my wife and Mrs. Pool.

The Court: All right.

The Witness: We proposed to purchase the 22 apartment buildings from Arteraft Builders, Inc. prior to the time that the land was purchased on which the apartments were built.

The Court: In other words, is this what you are saying: That you promised that if Arteraft did acquire the land and building the buildings, that you

(Testimony of William K. Murphy.)

four would buy them when they were built? Is that the idea?

The Witness: That is correct; yes, sir.

Q. (By Mr. Axelrad): Now, on the 70 duplexes did the same situation prevail?

A. Exactly, and we agreed to purchase them before Artcraft built them or before the land was purchased.

Q. While Artcraft was building them, it was your view that you already had an agreement with the corporation with respect to purchasing them?

A. Well, I felt we had a definite agreement. We had minutes covering them to the best of our ability. I thought [83] we had a contract, really.

Q. When these properties were all completed, that is, the 22 apartment buildings and the 70 duplexes, what happened?

A. Artcraft Builders, Inc. deeded them to Edward and Lottie Pool and Edna and W. K. Murphy.

Q. As what?

A. As our own separate estate, one-quarter interest.

The Court: Now, just a minute, so that I may follow you. At what dates are you speaking of?

The Witness: Well, they deeded us the 22 apartment buildings—I would have to refer to the record.

The Court: Well, approximately, for my purposes.

The Witness: I would say along about April, 1944. That would be a guess, however.

The Court: All right. Now, this question: I

(Testimony of William K. Murphy.)

think I recall your testimony that Cooke and Smith got out of the corporation. Was this while they were still in or was it after they got out?

The Witness: This was after they got out.

The Court: Now, just by way of review for me: When was it that they left the corporation and how did they leave?

The Witness: They left, to the best of my recollection, in May or June, 1943. Mr. Pool and myself and our wives, as I recall it, purchased their stock.

The Court: All right. Go ahead.

Mr. Axelrad: Incidentally, your Honor, the stipulation has all the dates concerning when these things were done.

The Court: I wasn't concerned with the exact dates. I was just wanting to review for the purpose of following the testimony.

Q. (By Mr. Axelrad): When these 22 apartment buildings and the 70 duplexes were completed and deeded to you and your wife and Mr. Pool and his wife, what did you as individuals do with them? Here you had all this property. What was the nature of your operation?

A. Well, we received the net rental after all expenses were paid on them.

Q. You mean you rented them?

A. We made an arrangement with Artcraft Builders, Inc. to take care of them and maintain them and rent them and do whatever was necessary to keep them up.

Q. What did Artcraft get for that?

(Testimony of William K. Murphy.)

A. Well, it varied. About a thousand dollars a month. I forgot what they got.

Q. They were paid a fee as a rental agent?

A. Yes, sir.

Q. Why did Artcraft serve as a rental agent on your property if it was yours? [85]

A. Well, they had the lawn men, the necessary painters, plumbers, superintendents. They had the Social Security, they had the entire setup and the organization to maintain the property and collect the rents and rent them for us.

Q. Did Artcraft report income from rental fees that they got from you and Pool and your wives?

A. Report them to whom?

Q. To the Government. Did they receive money that they reported as their income, acting as rental agent for you?

A. They reported any profit, I guess. I don't know that they report the income we got.

Q. I am not asking you that, Mr. Murphy. The question is this: You have testified you paid a fee to Artcraft. Now, I am asking you, did Artcraft report that fee on its return as income to it?

A. Yes, sir.

Q. Was the amount of that fee ever questioned in all of the tax controversies you have had relating to this property? To your knowledge has anyone raised any question about the reasonableness of the rental fee? A. No, sir.

Q. Were these apartments rented from month

(Testimony of William K. Murphy.)

to month or under lease, or in what manner did Artcraft carry out its job as rental agent? [86]

A. They were rented on a minimum of one year, and some of them were rented, I think, if I recall,—one was rented for three years.

Q. Were they all rented under leases?

A. Yes, sir.

Q. Written leases or oral?

A. No, they were all signed written leases.

Q. Now, in 1945 about the time of the end of the war, did you have any controversy with the rent control authorities concerning your method of leasing these properties?

A. In 1945 I was called to the Los Angeles office of the rent control; yes, sir.

Q. And for what purpose were you called?

A. They informed me that we weren't allowed under the rent control to accept the last month's rent. It is general procedure to accept the first and last month's rent when the lease is signed. They said that wasn't allowed under rent control.

Q. What did you have to do as a result of that discussion?

A. Well, we agreed with them. We gave the last month's rent back to all the tenants.

Q. I hand you some accounting paper with the heading, "Security Deposit, Tract 11451 and Security Deposit, Tract 11674." Can you tell the Court what this relates to? [87]

A. After I had my conference with the rent control, they instructed me—they thought that we

(Testimony of William K. Murphy.)

should return the rents, they felt that it wasn't according to the way they wanted it, and I told them that we would be happy to return them, and I went back to my office and had them go over the books and records and arrived at the amount owed each tenant on the last month of the rent we had collected under the lease, and told them to return it to them. And this shows our returning the rent to the people as we had been advised by the rent control.

Q. Was this prepared in your office?

A. Yes, sir.

Q. Under your supervision? A. Yes, sir.

Mr. Axelrad: I would like to offer this as a Petitioners' Exhibit.

Mr. Chehock: May I ask who prepared this schedule?

The Witness: Mrs. Woodruff.

Mr. Chehock: And who is Mrs. Woodruff?

The Witness: She is our bookkeeper.

Mr. Chehock: And she is under your supervision?

The Witness: Yes, sir.

Mr. Chehock: What year was this?

The Witness: That ran through 1945, as I recall it.

Mr. Chehock: When you say the last month, do you [88] refer to the twelfth month, or what?

The Witness: I refer to the last month's rent. If the lease was for three years, it was the 36th month; if it was two years, it was the 24th month;

(Testimony of William K. Murphy.)

and if it was for one year it was the 12th month. We had some leases that ran longer than 12 months.

Mr. Chehock: On the 70 and the 100 you had leases only for one year, didn't you?

The Witness: No. I think we had leases on the 11674 which—are you talking about the 70 and the 100? I couldn't say one way or the other where the longer lease came in.

Mr. Chehock: All of the leases you have now on the 70 and 100 are only for a year; is that right?

The Witness: I couldn't say without going through the leases.

Mr. Chehock: We have no objection, your Honor.

The Court: It will be received and marked in evidence as the next exhibit.

The Clerk: This is Exhibit 23.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 23.)

Q. (By Mr. Axelrad): What was the situation in 1945 with respect to costs of running rental property compared with the amount [89] of income you were getting?

A. In 1945 we were making a fair income, a fair return. The costs weren't so high in 1945. They were normal, I would say.

The Court: What costs are you talking about? Building costs, operating costs?

The Witness: Operating costs, that is, the maintenance and upkeep.

(Testimony of William K. Murphy.)

Q. (By Mr. Axelrad): The costs of running rental property, like taxes? A. Yes, sir.

Q. Painting, repairs, and so forth.

A. Upkeep of the lawns and so forth.

Q. What about in 1946 after the war had ended, early in 1946? Did this situation still continue? Were costs stationary?

A. Well, my recollection is that early in 1946 the costs hadn't jumped materially, I would say. Now, I am speaking of maintenance.

Q. Did any costs jump in the business of renting?

A. Well, your costs of construction, as I recall it——

Q. We are not talking about construction, Mr. Murphy. The cost of renting property that is already constructed. A. Not to my recollection.

Q. Taxes remained the same? [90]

A. No, taxes jumped.

Q. Was there any attempt on your part, on the part of Artcraft, for you to secure increased rentals, higher rental ceilings?

A. In 1945, as I recall it, or the early part of 1946, we made application to the—I forget the exact name. Anyway, it was Rent Control Board. We made application to increase our rent.

Q. What happened to that application?

A. They told us that we couldn't increase the rent, No. 1, because we had a lease on the property, and No. 2 was because they didn't think we were entitled to an increase.

(Testimony of William K. Murphy.)

The Court: They didn't think what?

The Witness: That we shouldn't be entitled to an increase at that time.

Q. (By Mr. Axelrad): What was your attitude about leases, leasing these properties at about that time as a result, if it is as a result, of their rejection of your application, by rent control?

A. What time are you speaking of?

Q. I am talking about 1946 or 1945, early in 1946.

A. Well, our attorneys, the fact of the matter is—I might qualify my last answer. Our attorney, Mr. P. M. Swaffield, went with me to the Rent Control Board and he stated [91] after he heard what they had to say, he advised us that we shouldn't sign any more leases except in the instances where we had one-bedroom apartments and good tenants.

Q. Which were those?

A. Those were the 22 apartment buildings. They were all one-bedroom apartment and we had couples there that had been there quite a while. He said the lease was all in favor of the tenant and it was not to our advantage to have a lease, that if the rent control came off, and he thought it would sooner or later, that we would be in better position to increase the rents.

Q. Going back to the time before you built the 22 apartments and the 70 duplexes—before Artcraft did—did anyone else besides Mr. Pool recommend rental investment property as a good source of income? A. Yes, sir.

(Testimony of William K. Murphy.)

Q. Who? A. Mr. C. E. La Bree.

Q. Who is Mr. La Bree?

A. Mr. La Bree was one of the officers of the Bank of America, and he handled our first loan on a tract, some five hundred twenty-five thousand dollars.

Q. What did he tell you?

A. He thought that we would be wise if we invested—built income property for investment and held it in our [92] name so that we would have an income in our old age.

Q. Did anyone else make any such recommendations? Did you make any study of the situation before you went into what seems to be a new kind of operation for you?

A. Well, I can speak for myself personally. I wanted an income that was guaranteed. The building business, I found, was pretty speculative, and Mr. Pool told me many times that you are up one day and down the other, and I was interested in establishing security for myself and my wife and family.

The Court: What do you mean by your use of the term "guaranteed?"

The Witness: How did I use it, your Honor?

The Court: You said you yourself would like an income guaranteed.

The Witness: Well, by "guaranteed" I meant an income from the investment on the rental properties.

Q. (By Mr. Axelrad): Are you using "guaran-

(Testimony of William K. Murphy.)

teed" in some relative sense? Was there anything sure about this rental income? Did anyone tell you that you were going to make that much money?

A. Nobody told me that we would have to make that much money, but I had had conferences with the Douglas Aircraft Company and others, and they stated that they would rent them, and the United States Navy. [93]

Q. Did Douglas Aircraft have anything to do with your decision to go into the rental business?

A. Well, I don't know——

Q. Were there any conferences with officials of Douglas with respect to getting more rental housing?

A. I had numerous conferences with officials of Douglas and the Federal Housing Administration relative to getting more rentals; yes, sir.

Q. Did you solicit their encouragement or did they solicit you?

A. Well, in 1944 I remember in one instance they solicited Mr. Pool and myself.

Q. What happened?

A. Well, the head of the rental department of the Douglas Aircraft at Long Beach called a meeting of Mr. McGovern, the director of the Federal Housing Administration, and Mr. Harold R. Thompson, who was the chief underwriter, and Mr. Simons, the chief valuator, and myself, and several other large building companies, and stated—I can't think of the name of the gentleman that was head of Douglas—that they wanted rental units and they

(Testimony of William K. Murphy.)

would like them as close to their plant as they could get them, and I think there were 600 priorities at that time were to be issued from Washington, and my recollection is that the Government issued us 200, and I forget who got the rest of them, but [94] it was all adjacent to the Douglas plant.

Q. Well, as a result of that meeting and further efforts on your part, what occurred?

A. Well, we built more rental units and made the engineering and went through FHA on another 54 apartment buildings, which we didn't build.

Q. What did you build at this time?

A. We built a hundred duplexes, 200 units.

Q. In a tract? A. 13163.

Q. What built that?

A. Artcraft Builders, Inc.

Q. And under what contract or understanding?

A. Well, it was the same understanding that we had on the other two tracts prior to the time that the land was purchased. We entered into an agreement that they would build the property, that we would purchase it.

Q. Was that reflected on the minutes of Artcraft directors' meetings, the understanding?

A. Yes, sir.

Q. Did the associates, that is, you and your wife and Mr. Pool and his wife, pay Artcraft anything for building these buildings, this 100 duplexes?

A. I thought we paid them $90,000.00.

Q. What did you pay them? [95]

A. I don't know.

(Testimony of William K. Murphy.)

Q. Well, Mr. Murphy, we have stipulated that there was a fee paid of thirty-five thousand-odd dollars, something in that nature. Does that figure strike a familiar chord?

A. Must have paid them that; yes, sir.

Q. What was the cost of building the 100 duplexes, in round numbers? That has been stipulated to, but just from your recollection.

A. You are talking about building the buildings?

Q. Yes, just the buildings, the cost of construction. Do you remember how much a unit it was?

A. I would say around $550,000.00.

Q. That would be $5,500.00 per unit?

A. Yes.

Q. If you were to build on a cost plus contract for the Government or for anybody else at that period, what would be the fee that officers of Artcraft would be willing to build for? What per cent was the Government paying, if you know, or what per cent would have been acceptable to Artcraft as a building fee?

A. Well, we always try to get ten, but we will take six per cent any time. I think the going fee at that time was cost plus six.

Q. From the Government? A. Yes, sir.

Q. Cost plus six per cent?

A. Yes, sir, subject to renegotiation.

Q. Did you and Mr. Pool and your wives advance money to Artcraft in order to secure any of the land involved in these rental units?

A. Yes, sir.

(Testimony of William K. Murphy.)

Q. Did you receive interest for that money?

A. I don't remember.

Q. You don't remember? A. No, sir.

Q. Now, when these 100 duplexes were completed, what occurred?

A. Well, we went through the same procedure and had Artcraft Builders manage them and rent them and maintain them and handle the upkeep and paid them a fee, cost plus a fee.

Q. In other words, you paid all of the costs of running these rental units to Artcraft, plus an additional net fee of something? A. Yes, sir.

Q. Now, when these 100 duplexes were completed, were they rented? A. Yes, sir.

Q. And were there leases taken?

A. Yes, sir. [97]

Q. How long were the leases, do you recall?

A. Minimum of a year. I am positive of that.

Q. I hand you here a group of papers that purport to be leases. Will you look at the first one and explain, if you know, to the Court what it is? Just the one on the top.

A. That is a lease between Artcraft Builders, Inc. and Mr. and Mrs. J. P. Treegarden for a period of one year, commencing on the 6th of April, 1946, and ending the 5th of April, 1947.

Q. What tract is that on, do you know?

A. That's the 100 apartments.

Q. That is the 100 duplexes? A. Yes.

Q. The last ones that you finished?

A. Yes, sir.

(Testimony of William K. Murphy.)

Mr. Axelrad: Off the record.

(Discussion off the record.)

The Court: On the record.

Q. (By Mr. Axelrad): When these 100 duplexes were completed, you have testified that they were deeded over by Artcraft to you, your wife, Mr. Pool and his wife. Did they continue to be rented?

A. Yes, sir. [98]

Q. Now, do you know what date or what month, at least, and what year you got title to the 100 duplexes, that is, you and your associates?

A. We got title I think February 1st.

The Court: February 1st of what year?

The Witness: Well, 1946. I think that was when it was, your Honor.

Q. (By Mr. Axelrad): I hand you here Exhibit 11, the minutes of the regular meeting of the board of directors of Artcraft Builders, Inc. on the 1st day of February, 1946. Is that the time you have reference to? A. Yes, sir.

Q. Will you read the resolution on page 146 of those minutes?

A. "Resolved that this corporation shall and does hereby grant to W. K. Murphy, Edna M. Murphy, Edward Pool and Lottie Pool as tenants in common, each owning an undivided one-quarter interest therein, Lots 1 to 100, inclusive, of Tract 13163 in the City of Long Beach, County of Los Angeles, State of California, as per map recorded in Book 264, page 9, of maps in the office of the County Recorder, Los Angeles County, California,

(Testimony of William K. Murphy.)

together with any and all buildings and improvements erected [99] thereon."

Q. What did that resolution refer to, which of the properties we have been discussing, if any?

A. The 100 duplexes.

Q. Was that resolution adopted?

A. "Upon motion duly made, seconded and unanimously carried, said resolution was adopted."

Q. Now, did you actually get a deed at that time, do you know?

A. A deed was made out at that time; yes, sir.

Q. Was it delivered to you?

A. Well, it was made out by our attorneys, Swaffield & Madden. It wasn't delivered to us at that time.

Q. It was not delivered? A. No, sir.

Q. What happened? When did you get a deed? This was February 1, 1946 we are talking about.

A. Well, my recollection was that—of course, this is from memory—they lost the deed or misplaced it and had another one made out.

Q. Did you ever see the deed that these minutes are talking about, the February 1,——

A. I saw it executed.

Q. Well, did something happen at the directors' meeting with respect to the deed? Was it there on exhibit [100] or was it made out afterwards?

A. As I recall, it was made out then and Mr. Pool and I signed it.

Q. Had it already been made out?

A. I don't recall that it was already made out.

(Testimony of William K. Murphy.)

Q. When did you sign it? A. Right then.

Q. And then was it delivered?

A. No, they were going to record it.

Q. Well, maybe you don't know what I mean by "delivered." Was it handed by an officer of the corporation to you or to Mr. Pool or your wives to symbolize the passing of title? Was there anything done with respect to the deed? It always is recorded, but that would be later. Can you remember whether anyone spoke any words about, "Here is title to this thing?"

Mr. Chehock: Your Honor, I believe this is quite leading. I am going to object on the ground that it is leading.

The Court: I doubt that it means very much, anyhow.

The Witness: Frankly, I don't remember.

Q. (By Mr. Axelrad): You don't remember what happened other than the resolution was adopted? [101] A. That's right.

Q. Was there anything that happened to a deed relating to this property that you do know something about? Was there a lost deed? You mentioned something about a lost deed.

A. Well, they were to record this deed.

Q. Who was to record this deed?

A. Our attorneys.

Mr. Chehock: What do you mean by "this deed?"

The Witness: The original deed of February 1, 1946. At a later date they called out——

Q. (By Mr. Axelrad): Who called out?

(Testimony of William K. Murphy.)

A. Phil Swaffield called our office, or we called him about something, and he brought up the subject of the deed, that he couldn't find it, did we have it, and we searched our files and our vault safe and we couldn't find it, and, to my recollection, another deed was made out then.

Q. Do you remember when, approximately?

A. Well, I would say it was about a month later or a month and a half, something like that. I don't remember exactly.

Q. Now, when did Artcraft Builders start building and when did you make your arrangements with Artcraft about building the 100 duplexes, what year? A. 1944. [102]

Q. What was the condition of the area in which you were building with relation to the deed for rental housing?

A. Well, it was very critical. The Navy wanted all we could build. Douglas wanted apartments, and some steel company over in Wilmington. I forget the exact name of it, but it was one of the big builders of ships over there.

Q. Well, after you started this tract, did you decide that the war was ending and that this would be a poor investment and that you ought to get rid of it as soon as you got title to it or as soon thereafter as might be feasible?

A. No. The head of Navy Housing offered to purchase the tract in 1945.

Q. Before it was completed? A. Yes, sir.

Q. Tell us in more detail what happened then.

(Testimony of William K. Murphy.)

Who was the head of Naval Housing? How did he come to you?

A. Well, I don't know how he came to us, but he came out originally and said he would rent all of the apartments that we had.

Q. Under a master lease?

A. No, he just sent out the naval officers and their wives and families, and we had some—I would say 200 apartments, or in that neighborhood, rented to them, and he came out upon numerous occasions and suggested that we rent more to them. We had a lot of Douglas employees and employees [103] from the shipyards there, and upon one occasion he suggested the Bureau of Harbor and Docks buy it, and we told him we weren't interested in selling it. He asked us, would we be interested in leasing it. I told him yes, for a period of five years, and he had, as I recall it, people from the Bureau of Harbor and Docks fly out here to the Roosevelt Base and went over the situation, and in the meantime the Navy came over. We were getting ready to start a hundred more at the same time we were starting the 100 duplexes, and the Navy sent some people over there and told us that they were going to take it away from us.

Q. What do you mean by take it away from you?

A. Well, condemn it.

Q. And pay you for it?

A. And pay us for it, yes. So they finally condemned the land and built 192 apartments of their own, and Mr. Scott said that if we had sold them

(Testimony of William K. Murphy.)

to them or had entered into a sale, they probably wouldn't have gone ahead and built them, and used ours.

Q. Why didn't you sell them?

Mr. Chehock: When was this?

The Witness: In 1945, on numerous occasions.

The Court : What was this numerous occasions?

The Witness: Well, at least Mr. Scott was out there on an average of about three times a week.

The Court: You mean some conferences?

The Witness: Yes, sir. Upon one occasion we had a conference with our attorney——

The Court: I am not sure that when this was, referring to conferences, that the context of the transcript will show.

Q. (By Mr. Avelrad): What do your numerous occasions refer to—conferences with the Navy?

A. Yes, sir.

Q. Conferences with respect to what?

A. On at least two or three occasions, purchasing the project.

Q. They wanted to purchase the entire 100 duplexes?

A. No, they wanted to purchase all we had.

Q. The 70 and the 22?

A. The 70 and the 22 and the 100; that is correct.

Q. What did you say?

A. We told them we weren't interested in selling.

(Testimony of William K. Murphy.)

Q. Because they wouldn't give you a big enough price?

A. No. Price didn't enter into it at all.

Q. You mean these were not for sale?

A. That's correct.

Q. Did anyone else ever offer to buy any of your investment property? [105]

A. Oh, we had at least, I would say, 50 or 60 of our tenants that were renting from us approached us.

Q. Did they come in a mass?

A. No, no. They would come in to pay their rent.

Q. And they would want to buy?

A. Yes, sir.

Q. And what was your answer?

A. They weren't for sale.

Q. Did real estate brokers ever ask you whether they were for sale? A. Yes, sir.

Q. I hand you here a document which purports to be a corporation grant deed, March 21, 1946. Can you identify this? A. Yes.

Q. What does it purport to deed to whom?

A. It deeds 100 duplexes to Edward Pool, Lottie Pool, William K. Murphy and Edna M. Murphy.

Q. Was that deed delivered to you?

A. Yes, sir.

Q. Does the recording stamp show on that?

A. Yes, sir.

Q. You say, though, that there was a deed before this that was lost, the February deed.

A. Yes, sir. [106]

(Testimony of William K. Murphy.)

Q. This was the deed that was actually recorded?

A. Yes, sir, that was recorded.

Mr. Chehock: I have no objection to it going in.

The Court: It will be received and marked as the next exhibit.

The Clerk: Exhibit 24.

(The document above referred to was received in evidence and marked Petitioners' Exhibit No. 24.)

The Court: We will take an intermission.

(Short recess taken.)

The Court: On the record.

Q. (By Mr. Axelrad): Mr. Murphy, when you and your associates got title to the 100 duplexes in 1946, the war was over, wasn't it? A. Yes, sir.

Q. Did that alarm you as far as the quality of your investment in these rental units? Did you feel that you ought to sell immediately?

A. No, sir.

Q. Well, were you actively looking for other similar investments or did you feel that you had just the right amount?

A. Well, several months after—we were working on a job at that time, the preliminaries to building some more rental units.

The Court: Who was working on it? [107]

The Witness: Mr. Pool and myself.

The Court: I think it might be helpful just to note at this time that I have individuals in this trial and corporations, and sometimes I might not

(Testimony of William K. Murphy.)

know whether you are talking about the corporation or whether you are talking about individuals.

When you say "we," you are talking about officers of the corporation and you are talking about individuals. So you might take note of that and be very careful to make it clear in your testimony that when you are talking about Pool and Murphy as individuals, you indicate so that I will not have any difficulty as to what you mean.

The Witness: Yes, sir.

The Court: I may have to draw some conclusions myself, but at least I will know what you mean.

Q. (By Mr. Axelrad): I hand you here a document that is labeled, "Tentative Map, Tract No.—, in the County of Los Angeles, Type No. 7," and it is approved by W. K. Murphy and purports to be the signature of the secretary, dated April 10, 1946.

Will you explain to the Court what that document is, if anything?

A. This is a proposed tract map of a proposed development of duplexes that Artcraft Builders, Inc. proposed to build for Pool & Associates, Pool, Murphy and our wives. [108] This was in April 1946.

Q. Where was that tract to be located?

A. This tract was on Central Avenue and Rosecrans in Compton, California. That is between Los Angeles and Long Beach.

Q. Was it to essentially the same kind of build-

(Testimony of William K. Murphy.)

ings that you had on your 100-duplex tract and your 70? A. Exactly the same.

Q. You intended to have the corporation build for you and then rent it? Was it to be a further investment, in other words? A. Yes.

Q. What happened to your plans? Did you ever build it?

A. We filed the application for subdivision with the Federal Housing Administration.

Q. When?

A. As I recall it, in the latter part of April or early part of May. It was approved by the Federal Housing Administration in the middle of May and we found out there were oil leases on the property, so we gave it up after we spent some eight or nine hundred dollars on the project.

Q. What did the oil leases have to do with giving it up? A. Well, you couldn't finance it.

Q. Why not? [109]

A. Well, they wouldn't finance it with an oil lease on the property.

Q. Someone had the right to drill oil there?

A. That's right.

Mr. Axelrad: Some of these things might not be self-evident. At least I wasn't sure myself. I offer this as Petitioners' Exhibit 25.

The Court: Any objection?

Mr. Chehock: No objection.

The Court: Received and so marked.

(The document above referred to was re-

(Testimony of William K. Murphy.)

ceived in evidence and marked Petitioners' Exhibit No. 25.)

Q. (By Mr. Axelrad): When you were negotiating and deliberating about the tract that was never built, that was in April of 1946? A. Yes.

Q. You had already secured title to the 100 duplexes? A. Yes, sir.

Q. What happened in January or February of 1946 relating to these tracts, the disposition of them, the sale of them, if anything?

A. Nothing that I recall.

Q. Did you have any further inquiries about sale?

A. Yes. We had a broker come down in February of 1946, I think. [110]

Q. A broker?

A. Yes, a real estate broker came to our office in February of 1946, to the best of my recollection.

Q. And who was that real estate broker?

A. Mr. Boland.

Q. What did he want?

A. Originally, he said he had a purchaser for the entire tract.

Q. Which tract are you talking about?

A. Well, the 70 duplexes and the 100 duplexes and the 22 apartment buildings.

Q. He had one purchaser for all three tracts?

A. That's what he said.

Q. What did you say to him?

A. Told him they weren't for sale.

Q. You say this was in February of 1946?

(Testimony of William K. Murphy.)

A. To the best of my recollection.

Q. Did Mr. Boland come back again?

A. He came back upon numerous occasions.

Q. What did he want on numerous occasions?

A. He wanted us to sell the property.

Q. Did he have a buyer?

A. He didn't say whether he did or not after the first one, but we told him we weren't interested in selling.

Q. Well, you finally did sell them, didn't you?

A. Yes, sir.

Q. What happened? Under what circumstances did you finally sell the 70? The 70 duplexes were sold first, were they not? A. Yes, sir.

Q. Under what circumstances did you finally decide to sell?

A. Well, Mr. Boland kept coming down and telling us that he could sell them, and we had a conference in the early part of May, as I recall. I am speaking now of the 70 duplexes.

The Court: What year?

The Witness: 1946. We had a conference with Mr. Erwin Lampe of Arthur Young & Company, and the resident partner. It was a Scotch name and I don't recall the name of the gentleman, but they had gone over the property, that is, the records and the books, and they told Mr. Pool—Mr. Pool was at the conference also, along with myself—and they told us that in their opinion that property had practically doubled in the last 90 days and that in view of the fact that we could not increase the

(Testimony of William K. Murphy.)

rents, that it seemed to be that we could better ourselves along investment lines by selling the property and investing it in other lines of security.

Q. (By Mr. Axelrad): What do you mean when you say the property had [112] practically doubled? You mean the resale price, the fair market value?

A. Fair market value, yes.

Q. Were you losing money on this property?

A. No, sir.

Q. Wasn't it still a good long-term investment?

A. Well, they seemed to think that it wasn't for the return as compared with the actual value of the property at that time.

Q. Well, was the proposal that you should sell so that you could put it in property that would give you a higher return?

A. The proposal to sell was that we should sell the property. I invested all my money in stock and bonds.

Q. Is that what they suggested that you do?

A. They didn't suggest that we invest in stocks and bonds, as I recall it, no.

Q. These had cost you what, each one of the duplexes with the land?

A. Approximately $6,000.00 apiece.

Q. And what did they tell you they might be sold for?

A. They said in the neighborhood of eleven or twelve thousand dollars.

Q. In other words, you would double your costs?

A. Yes, sir. [113]

(Testimony of William K. Murphy.)

Q. And the rent as fixed on your cost price, was it more or less a fair return on that?

A. Yes, sir.

Q. So that as a result of the rise in the market, you couldn't take advantage of it without disposing of the property and reflecting it in income?

A. That's correct.

Q. What did Mr. Boland have to do with this? You say Aruthr Young & Company gave you this advice. Where did Mr. Boland fit into the picture?

A. Mr. Boland came down on numerous occasions, and finally the last time he came down, which I think was the early part of May, he said that he could sell the properties for $12,000.00 apiece.

Q. How did he know he could?

A. I don't know.

Q. Was he an experienced broker? Would you just let anybody tell you something and then put it on the market?

A. No, not exactly. It was after that that we talked to Mr. Lampe and Arthur Young & Company.

Q. You mean they confirmed his suggestion?

A. Yes, sir.

Q. What was Mr. Boland's interest in this thing?

A. Boland's interest in it, I presume, was collecting a commission. [114]

Q. He wanted something to sell?

A. Yes, sir.

Q. Did real estate agents customarily go around

(Testimony of William K. Murphy.)

soliciting property to sell? Is that part of their work? A. Yes.

Q. He did a lot of soliciting?

A. Yes, as far as we were concerned, I would say he did.

Q. You had the hundred duplexes and the 70 duplexes and the 22 apartments. Did you let him sell them all?

A. No, sir. We told him he could sell the 70 duplexes.

Q. Did he want to sell them all?

A. He wanted to sell them all, yes.

Q. You let him sell the 70 duplexes?

A. Yes, sir.

Q. What were the arrangements you made with him about selling them?

A. We agreed to pay him the regular brokerage, which was five per cent. Mr. Boland said, and he offered, that if we would allow him the use of our office, because there wasn't any office space within three miles of there, and he said he would have to be close to the property if he sold it, and light and gas and one thing another, that he would sell them for us for a net of $500.00 and he would pay for all the credit reports and his company would handle all [115] the sales and do all the paper work and open the escrows and whatever was necessary to sell the property.

Q. Who was to do the advertising?

A. He was.

(Testimony of William K. Murphy.)

The Court: Do you mean he was to receive $500.00 on each sale; is that correct?

The Witness: He was to get $500.00 on each sale; yes, sir.

Q. (By Mr. Axelrad): Do you mean net after paying all these things or get $500.00 net from you and pay out of the $500.00 these other things?

A. He was to get $500.00 from us. The commission from us on the first tract would be $540.00.

Q. At five per cent? A. Yes.

Q. You gave him $500.00 instead?

A. And he was to pay all his expenses.

Why didn't you give him $540.00?

A. Well, he wanted to use our office.

Mr. Chehock: Here is another example of the word "our." I don't know wheher Artcraft's office or Murphy's office or Pool's or whose.

The Witness: Artcraft Builders, Inc. and Edward Pool and Associates. [116]

Q. (By Mr. Axelrad): You both had offices in the same place? A. Yes.

Q. You kept your books there? A. Yes.

Q. In this case "our" refers to all of you?

A. Yes, sir.

Q. You say you let him use your office because there was no other office near?

A. Yes, within two or three miles.

Q. Where was your office with respect to the tract with the 70 duplexes on it?

A. It was in the center of it.

Q. Right in the center of the tract?

(Testimony of William K. Murphy.)

A. Part of it was south of the office, part of it was west, and part of it was north of the office.

Q. In other words, you were right in the middle of this tract, in a sense? A. Yes.

Q. Why was it necessary that he have an office near the tract? Why couldn't he have his office any place?

A. Well, he said the people would come to the tract to see the buildings, and he wanted to be situated close by where he would be handy to show them to them.

Q. You gave him $500.00 instead of $540.00, and let him [117] use your office? A. That's right.

Q. He paid everything else? A. Yes, sir.

Q. Did you have a telephone installed, or did he have a telephone installed in the office, or did he use yours?

A. I am pretty sure he used ours.

Q. Why did he do that?

A. That was part of the $40.00.

Q. Did you ever pay any of the advertising?

A. No, sir.

Q. Did you make out any ads?

A. Never, no, sir.

Q. Did you ever show any of these houses?

A. Never. Never showed a one.

Q. Did anybody in Artcraft organization ever show any to your knowledge?

A. Not to my knowledge.

Q. Did your wife ever come down and help out on the sale?

(Testimony of William K. Murphy.)

A. I don't think my wife was ever in the office over once.

Q. Once during this period or once ever?

A. Once ever.

Q. Did your wife ever have a real estate [118] broker's license? A. No, sir.

Q. Never been associated with real estate of any kind? A. No, sir.

Q. What about Pool? Was he there?

A. Well, we were there part of the time. We weren't there all the time.

Q. Were you out of town during any of this period? A. Quite a bit; yes, sir.

Q. Do you remember any specific trips or any specific dates or periods?

A. I went trout fishing in May up in the High Sierras for approximately two or three weeks.

Q. Was this part of the time that these duplexes were being sold?

A. Yes, sir. Then I went to Chicago and Rochester, Minnesota the latter part of August or the early part of September. I was gone, I would say, a week to ten days.

Q. All while sales were occurring?

A. Yes, sir.

Q. Was Pool there the whole time or at least in town? A. No, he was in Cincinnati.

Q. When did he go to Cincinnati, if you remember?

A. He was in Cincinnati in May of 1946.

Q. While these duplexes were being sold? [119]

(Testimony of William K. Murphy.)

A. Yes, sir.

Q. Was he here when the agreement was made to sell them? A. I think he was; yes, sir.

Q. Wouldn't he have had to give his authority to sell? A. Yes.

Q. He was here and gave his authority?

A. Yes.

Q. He left while they were being sold?

A. He left while they were being sold. I know he was in Cincinnati in May.

Q. Did your office force or Artcraft Builders, Inc., or any of your associates have anything to do with selling these? A. No.

Q. Did your secretary show houses or make out contracts? A. No, sir.

Q. Did you ever call for credit reports?

A. No. Mr. Boland was to call for all the credit reports, too; that is, the Boland Realty Company.

Q. I know who was to do it, but who actually did it? A. He did.

Q. You don't know who did it, but you know you didn't do it, and you know your office didn't do it. A. That's right.

Q. How long did it take to sell the 70 duplexes, do [120] you know?

A. I don't remember. I don't think it took him very long. I would say, just as a guess, about four or five weeks, if it took him that long.

Q. Then you still had the 22 apartments and the hundred duplexes? A. Yes, sir.

Q. Did Mr. Boland want to sell those, too?

(Testimony of William K. Murphy.)

A. Yes, sir.

Q. What did you tell him?

A. We weren't interested in selling them.

Q. So what did he do, sit in your office waiting for you to change your mind? A. No, he left.

Q. He went about his business?

A. I think he went back East.

Q. Then what happened?

A. Well, I don't remember exactly. He came back then along in August sometime, back from the East, and he inquired about selling the hundred.

Q. What do you mean by "inquired?" What did he do?

A. Well, he wanted us to sell them.

Q. What arguments did he use at this time, if any?

Mr. Chehock: Who are you quoting?

Mr. Axelrad: Mr. Boland. [121]

Q. Mr. Boland came back in August and wanted you to sell the hundred?

A. Some time in August or July.

Q. Late summer? A. Yes.

Q. What did he say he wanted?

A. He wanted us to sell the hundred and the 22 apartment buildings in the first tract.

Q. What did you say?

A. We told him no, we weren't going to sell them, we were going to hang onto them.

Q. Did he have to persuade you to sell them?

A. Yes, I would say he did.

Q. Why did he? What was the problem about

(Testimony of William K. Murphy.)

whether you should sell or not? What arguments did he use?

A. Well, he sold the first—that is, the 70 duplexes—I think for $10,800.00.

Q. What did you pay him to sell those?

A. $500.00 each.

Q. And he made $35,000.00 from you?

A. Yes, sir.

Q. Less whatever his expenses were.

A. Yes, sir.

Mr. Chehock: On the record, I believe counsel stipulate it was $11,000.00 instead of $10,800.00.

Mr. Axelrad: As the sale price. The stipulation will show whatever it was.

The Witness: It was $10,800.00.

Mr. Axelrad: Well, the sales price—we might as well clear that up. We have stipulated they were sold for $11,800.00.

The Witness: My recollection is that they were sold for $10,800.00.

Mr. Axelrad: For the purposes of this case, you are bound by the stipulation. Your books show $11,800.00.

Q. (By Mr. Axelrad): Now, you paid him $35,000.00 for selling those and you say it took roughly six weeks. He came back in August, and what did he say to you?

A. He wanted to sell Jacinto Way, that is, the 22 apartment buildings and the hundred apartment buildings, and we told him we weren't interested in selling them.

(Testimony of William K. Murphy.)

Q. Well, you sold them. How did you sell them?

A. He came back on several different occasions, and finally we decided we would sell them.

The Court: Who decided?

The Witness: Mr. Pool and myself.

Q. (By Mr. Axelrad): Did you decide to sell because he came back so many times and you felt sorry for him, or what? [123]

A. Oh, no. We decided to sell them because we had been advised it ceased to be a good investment. The return on what the building was worth didn't figure out right, so we were advised.

Q. Were these still under rent control?

A. Oh, yes, and we weren't allowed to raise the rent.

Q. Had you expectations that rent control would go off after the war?

A. We thought it would go off right after the war; yes, sir.

Q. What happened? A. It didn't go off.

Q. That made a difference in your thinking about the investment possibilities?

A. Absolutely.

Q. When you finally decided to sell, what were the arrangements made and concerning what duplexes? We have the 70 sold now, and we are talking about the hundred and the 22.

A. Well, it was the same arrangement, as I recall it, that we had on the 70 duplexes.

Q. Same arrangement with respect to what tracts or houses? A. The hundred duplexes.

(Testimony of William K. Murphy.)

Q. What about the 22? [124]

A. Well, we didn't sell the 22.

Q. You refused to sell the 22? A. Yes.

Q. Why did you refuse to sell those and agree to sell the hundred?

A. They were all single-family rentals and they weren't allowing us any rental for children, and in one apartment, for instance, up there in the hundred we had nine people living in the apartment, and over 50 per cent of them I think we had children in them.

Q. You mean you thought that for a long-term investment the 22 were better than the hundred because they were smaller?

A. One-bedroom, yes.

Q. You wouldn't have the problem with children? A. That's right.

Q. So you decided to sell the hundred?

A. Yes.

Q. And you did sell the hundred? A. Yes.

Q. And you sold through Mr. Boland?

A. Boland Realty Company.

Q. Did you give him an exclusive contract or agreement, or what were your arrangements with him?

A. We agreed to pay him $500.00, and he was to pay [125] all of his expenses, $500.00 a building.

Q. Did your lawyer draw up a contract?

A. I don't remember him drawing one, no.

Q. Did you have an exchange of letters?

A. No, I don't know whether we did or not.

(Testimony of William K. Murphy.)

Q. You do know you sold them? A. Yes.

Q. You know you paid him $500.00?

A. Paid him $50,000.00; yes, sir.

Q. At that point you had paid him $85,000.00 for selling the two tracts? A. That is correct.

Q. Did you help him out? He was in your office. You were down there some of the time, I assume. Did you wait on some of the trade as it came in?

A. Not that I recall. He had two salesmen out on the tract, two brokers, as I remember.

Q. Working for him? A. Yes.

Q. Did you ever pay them?

A. No, we never paid the other two men.

Q. You had no connection with them?

A. No.

Q. Did you pick them out for him? A. No.

Q. You say that to the best of your recollection you never showed the properties?

A. No, I have never showed them. I am positive of that.

Q. You are positive about that? A. Yes.

Q. What aren't you positive about?

A. If somebody came in and they were busy, they might have said something about an apartment building and I may have answered their question or something like that.

Q. You may have answered a casual inquiry, but you are not sure? A. That's right.

Q. You never showed any apartments?

A. No.

Q. Did you ever sign any sales contract?

(Testimony of William K. Murphy.)

A. No.

Q. Did you sign "Boland Realty Company by W. K. Murphy," or anything like that?

A. If I did, it was only once, if I ever signed it.

Q. Do you remember whether you ever did?

A. No, sir.

Q. What about Mr. Pool? Was he out showing the property? A. No, sir. [127]

Q. Was he in the office helping sign contracts?

A. No, sir.

Q. Who got up the escrow when you went into escrow? You had to have escrow instructions. Who drew those up? Did you? A. No.

Q. Mr. Pool? A. No.

Q. Your secretary? A. No.

Q. Anybody in your organization? A. No.

Q. Did your wife? A. No, sir.

Q. What about the advertising on this second tract? Did you prepare the ads?

A. I never prepared the ads on any of the tracts.

Q. Did you see the ads?

A. I saw them in the newspaper if I was in town.

Q. Do you remember whether you ever saw any of them? A. I couldn't say definitely, no.

Q. You don't know whether you saw them or not?

A. I don't know. If I was in the city, I probably saw them.

Q. You don't remember what they said? [128]

A. No, sir.

(Testimony of William K. Murphy.)

Q. If you had wanted to sell these yourself, do you suppose you could have?

A. I don't know whether we could or not. I don't know whether we would be required to be real estate brokers or not.

Q. Do you suppose you could have hired somebody with a broker's license as an employee?

A. Oh, yes.

Q. You have built tracts for sale before, have you not, as officers of Artcraft? A. Yes.

Q. Did Artcraft ever employ a broker to sell?

A. Employed six or eight of them to sell.

Q. When they were working for your corporation, what would they be paid? Five per cent?

A. No. They were selling houses. They only had to get $50.00 down on the house to $200.00. I forgot what they got paid. I think it was a hundred dollars a house. It was under contract, however, but Artcraft paid for all the advertising.

Q. Do you know whether it is customary for a speculative builder to pay a straight five per cent commission to an independent broker or is it customary to do something else?

A. Well, a speculative builder usually agrees on so [129] much a building, like we paid, I think, for houses, either 50 or a hundred. They agree on a price. They don't usually pay any five per cent, no.

Q. It would be a very good business if they could get five per cent for disposing of things like that, wouldn't it? A. Yes.

Q. Why didn't you hire somebody with a bro-

(Testimony of William K. Murphy.)

ker's license and pay them a hundred instead of $500.00?

A. Because we weren't interested in engaging in the selling business.

Q. What else is there to it besides getting the customers? All you have to do is put an ad in the paper and take them out there and show them the place. Is there anything else? A. That's all.

Q. You spoke about credit reports. Do you do that?

A. Boland Realty Company got a credit report on the people and they drew up escrow papers.

Q. Did all these escrows move smoothly?

A. Oh, no.

Q. What would happen, do you know?

A. Well, some of them would blow up, I guess, while they were in escrow.

Q. Sometimes these things had to be sold more than [129-A] once? A. Oh, yes.

Q. It is your testimony, as I understand it, Mr. Murphy, that as late as 1946 you were actively engaged, you and your associates, Mr. Pool and your wives, in attempting to build more rental units?

A. We filed application for a subdivision with the Federal Housing Administration and they wrote us a letter approving of it.

Q. But by August of 1946 you had disposed of or offered to dispose of two very substantial pieces of your holdings. A. Yes, sir.

Q. What brought about that great change between April and August? In fact, between April

(Testimony of William K. Murphy.)

and May, because in May you put the 70 duplexes on the market; isn't that correct?

A. Yes, sir.

Q. What happened?

A. Well, we were advised that the price of the building, the value of the property, each individual duplex, was so high at that time that the return on it didn't warrant keeping it. We were advised that by Arthur Young & Company's resident partner and Mr. Lampe.

Q. What did you do with the money you got out of the 70 apartments and the hundred duplexes?

A. Well, I invested it in stocks, Guaranty Trust of [129-B] New York and U. S. Steel, Kennecott Copper.

Q. Did you get a higher return than you did from your real estate?

A. I don't remember. I think I wound up eventually with a loss.

Q. That wasn't anticipated, I suppose, when you bought the stocks. A. No, sir.

Q. Did you continue actively, through your corporation or otherwise, in any kind of real estate operation? A. No, sir.

Q. What was your status at that point?

A. We had retired. You mean after we sold them?

Q. Yes. A. We were retired.

Q. You were in retirement? A. Yes, sir.

Q. How long did that continue?

A. Five years.

(Testimony of William K. Murphy.)

Q. You mean until 1951?

A. I think it was October 1950 or November 1950.

Q. What happened then? Did you start in the real estate business?

A. No. we started building again, Artcraft Builders.

Q. Your corporation started building again?

A. Formed a new corporation.

Q. Formed a new corporation? A. Yes.

Q. You took stock in it? A. Yes.

Q. You became an officer? A. Yes.

Q. And the corporation a building organization?

A. Yes.

Q. And you became an employee of the corporation? A. Yes.

Q. That was when you came out of what you call retirement?

A. Yes, sir. Let me qualify that. We did build a business building in the meantime.

Q. A business building? A. Yes.

Q. Where was that?

A. Across the street from a market building in a business block we owned.

Q. Where? A. That was in Long Beach.

Q. When did you build the business building?

A. We built the business building in 1948, I think.

Q. Who built it? [129-d]

A. Mr. Pool and myself. Artcraft Builders, Inc. built it for us.

Q. And deeded it over to you?

(Testimony of William K. Murphy.)

A. No, we had the property in our own name.

Q. You bought the land first?

A. We bought the land three or four years previously.

Q. And Artcraft put a building on it?

A. Yes.

Q. Did you pay Artcraft for putting the building on it? A. I don't remember.

Q. What was the nature of the building? Why did you build it?

A. Well, we bought the business lot and we built it for an investment.

Q. What kind of an investment is a business building? You mean to rent out stores?

A. Yes, sir.

Q. Did you do that? A. Yes, sir.

Q. Did you rent them? A. Yes, sir.

Q. And did you decide a few months or six months after you had built it that all of a sudden you would sell it? A. No, sir.

Q. Did you ever sell it? [129-E]

A. Yes, sir.

Q. Why did you sell it?

A. Because it was foreclosed.

Q. Why was it foreclosed?

A. Well, we had made a bad investment in this building project that I just referred to in the new corporation.

Q. In other words, it was a forced sale because you had to get your money out?

A. That's right. We had to get our money out,

(Testimony of William K. Murphy.)

and we sold it prior to the foreclosure, I would say. The Bank of America agreed to hold off on the foreclosure until it was sold.

Q. When was it sold? A. 1952.

Q. In other words, you had it about four years?

A. Yes, sir.

Q. When there was a forced sale.

A. Yes, sir.

Q. Did you ever own any other property, you and Mr. Pool and your wives and Associates together, besides the three tracts were are talking about?

Mr. Chehock: Counsel, if you don't mind, rather than going back into this, he mentioned about forming a new corporation and that a building was built and that there was a foreclosure. Was this building [129-F] built by this Artcraft we are talking about in this lawsuit or the Artcraft in the other corporation?

The Witness: No, sir, this same one that we are talking about in this case.

Mr. Chehock: Was that referred to as a bank building?

The Witness: That is what I refer to it as.

The Court: As a bank building?

The Witness: Yes, sir.

Q. (By Mr. Axelrad): It had other things besides a bank in it, did it not?

A. Yes. It had six other businesses.

Q. In other words, there were seven stores, a bank and six others? A. Yes, sir.

(Testimony of William K. Murphy.)

Q. What else was in there besides the bank?

A. Well, there was a furniture store, a hardware store, a wet wash laundry, offices.

Q. Sporting good? A. Sporting goods.

Q. Those were rental properties as far as you were concerned? A. Yes, sir.

Q. You refer to that building as a bank building? A. Yes. [129-G]

Q. Now, did you own anything else while you held the 70 duplexes, the 22 apartments and the 100 duplexes before you sold any of them? Did you own anything else as associates, or as an individual, for that matter?

A. We owned the lot we built the bank building on.

Q. Anything you built anything on besides the bank building. You had a market, didn't you, in connection with a drug store? A. Yes, sir.

Q. Where was that located?

A. In Long Beach.

Q. Where in Long Beach?

A. Across the street from the bank building.

Q. Was that meant to service your duplexes and apartments? A. Yes, sir.

Q. Did Arteraft build that? A. Yes, sir.

Q. It was deeded to the individuals?

A. I think it was built under our name.

Q. Built on your land? A. Yes, sir.

Q. And you paid Arteraft something for building it? A. I don't remember. [129-H]

Q. Now, when was that built?

(Testimony of William K. Murphy.)

A. That was built in the summer of 1944.

Q. And after the war did you decide to sell that and get what somebody told you would be a capital gain?

A. No, sir. We were getting some $38,000.00 or $40,000.00 a year rent for it, and we still owned it.

Q. You still owned it? A. Yes.

Q. You never sold it? A. No, sir.

Q. You have held that about nine or ten years up to date; is that correct?

A. About eight years.

Q. Why was that a good rental investment? There was rent control on it too, wasn't there, or was there?

A. Well, that was on a percentage lease. In other words, the higher the commodities went the more rent we received. It is still on that basis.

Q. It had a built-in protection against inflation because it was a percentage lease? A. Yes, sir.

Q. The OPA didn't object to that kind of a lease, apparently? A. No, sir.

Q. I hand you a carbon copy of what purports [129-I] to be a letter to Douglas Aircraft, dated January 4, 1945. Can you identify that, who wrote it, and under what circumstances?

A. Our general auditor, George Clark, wrote this.

Q. How do you know?

A. Well, I know his initials down here, "G. C." He is the only auditor we ever had.

Q. To whom did he write it?

(Testimony of William K. Murphy.)

A. He addressed it to the Douglas Aircraft Corporation in Long Beach, attention Mr. Milner, the Housing Director. This letter was written at my direction.

Q. What was the subject?

A. This was after the conference we had with the FHA officials and the Douglas people at their plant that I referred to in my testimony here.

Q. What was the date?

A. January 4, 1945.

Q. What did you tell Douglas in January 1945 as evidenced by that letter?

A. Well, we tell them, "We will hold the units for Douglas employees until otherwise advised by you."

Q. In other words, you would rent exclusively to them?

A. Until advised, you know, that they couldn't take any more of them.

Mr. Axelrad: I would like to have this marked for identification as an exhibit. [129-J]

The Court: Any objection?

Mr. Chehock: No objection.

The Court: It will be received and marked as the next exhibit.

The Clerk: It will be No. 26.

(The document referred to was received in evidence and marked Petitioners' Exhibit No. 26.)

Q. (By Mr. Axelrad): I hand you another letter dated January 9, 1945. Will you identify that?

(Testimony of William K. Murphy.)

A. This is a letter addressed to the Douglas Aircraft Corporation, attention Mr. Milner, the Housing Director.

Q. That is the same man that the other letter was written to? A. Yes, sir.

Q. Who signed that letter? A. I did.

Q. You wrote it? A. Yes, sir.

Q. What do you say in there?

A. Well, "Supplementing our letter of recent date relative to our proposed development of housing units to supply Douglas employees only, we wish to submit the following policy which will be adopted 100 per cent by this company. [129-K]

"We propose to build 400 two-bedroom units, which will be exclusively for Douglas employees, and further, in the event an employee of Douglas who is living in our property terminates his employment with your company, we will use every effort to evict him from the property.

"We will hold the entire 400 original rentals for Douglas employees and for a period of a minimum of two years, all of the rerentals will be exclusively for employees of your company and will be sent to us with their referral slip from you.

"Thanking you for your consideration, we are,

"Artcraft Builders, Inc.,

"W. K. Murphy."

Q. You speak of 400 two-bedroom units. What does that refer to? You didn't have 400 two-bedroom units, did you?

A. That is the hundred duplexes that we refer

(Testimony of William K. Murphy.)

to and the hundred that the Navy condemned on us.

Q. In other words, you planned to build 400, but you only completed 200 because the Navy took 200? A. That's right.

Q. You were offering to hold them all for two years? A. Minimum of two years.

Q. What happened as a result of that letter? Did you have any conferences?

A. Well, they started sending us referral slips [129-L] as soon as the apartments were built, and we rented to them until they couldn't send us any more.

Q. In other words, you were operating under that agreement until the war ended?

A. That's right.

Mr. Axelrad: I would like to offer this letter of January 9 as Petitioners' Exhibit No. 27.

Mr. Chehock: No objection.

The Court: It will be received and so marked.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 27.)

Q. (By Mr. Axelrad): Mr. Murphy, you testified that the 70 duplexes were sold beginning in May of 1946 and the hundred beginning in August or thereabouts of 1946, but you refused to sell the 22 because they were a more desirable investment property because they were smaller and you could exclude children and pets, I gathered your testimony was; is that correct?

A. I don't know exactly. We started to sell the

(Testimony of William K. Murphy.)

70 sometime in May and we started to sell the hundred around the latter part of August.

Q. When did you sell the 22 and under what circumstances?

A. Well, the 22, we sold those in the latter part of 1949 and 1950. [129-M]

Q. When were those built, did you say?

A. They were completed in November 1943.

Q. You hold those six or seven years?

A. Yes, sir.

Q. Under what circumstances did you sell those?

A. Well, we hired a broker and paid him a flat five per cent commission.

Q. What broker did you hire, if you recall?

A. Marshall Smith.

Q. Did he advertise them? A. Yes, sir.

Q. Did he hire people to work for him or did he handle them himself?

A. I think he hired people. At least I know he had one person working for him.

Q. Why did you decide to dispose of those in 1949 and 1950?

A. Because we had approximately 15 to 20 vacancies there all the time.

Q. You mean they were becoming hard to rent?

A. Yes, sir.

Q. Why was that?

A. Well, there were a lot of houses built that were sold with a low down payment and people moved.

Q. Is it your testimony that you disposed of

(Testimony of William K. Murphy.)

[129-N] those because they were a poor investment?

A. Yes.

Q. Because of lack of permanent tenancy?

A. Yes, sir.

Mr. Axelrad: That completes my examination of Mr. Murphy.

The Court: Well, I suppose that we might suspend then until 2:00 o'clock.

(Whereupon, at 12:30 p.m., a recess was taken until 2:00 p.m. of the same day.) [129-O]

Afternoon Session, 2:00 p.m.

The Court: All right.

Whereupon, William K. Murphy, called as a witness for and on behalf of the Petitioners, having been previously duly sworn, resumed the stand and testified further as follows:

Mr. Axelrad: If your Honor please, when we recessed for lunch I had completed the direct examination of Mr. Murphy. We have one witness that is here today and has to be in court in Long Beach tomorrow and probably the next day. If the Court approves, we would like to call him before the Government has an opportunity to cross examine Mr. Murphy so that we can be sure to get his testimony in when he is available.

The Court: You gentlemen know your case better than I do at this time.

Mr. Chehock: Your Honor, I don't like to have an interruption in the record because it doesn't

make for a good record, but in view of the situation, I wouldn't urge the objection.

The Court: All right. You may call the witness.

Mr. Chehock: I think the record should clearly show the fact that Mr. Murphy has left the witness stand and cross examination will be had at a later [130] date after this witness has concluded.

The Court: The record will show that.

(Witness temporarily excused.)

Mr. Axelrad: Mr. Block, will you take the stand?

Whereupon,

THOMAS H. BLOCK

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your name, please?

The Witness: Thomas H. Block.

Direct Examination

Q. (By Mr. Axelrad): What is your occupation, Mr. Block?

A. I am a plastering contractor.

Q. How long have you been a plastering contractor? A. About 25 years.

Mr. Chehock: Do you mind speaking up so I can hear you?

The Court: Keep your voice up.

The Witness: Surely. 25 years.

Q. (By Mr. Axelrad): Did you ever do business with Artcraft Builders, Inc.?

A. Yes, I did. [131]

Q. In what capacity?

(Testimony of Thomas H. Block.)

A. As plastering contractor.

Q. Approximately when?

A. Well, it was on and off in the years between 1942 and 1943, I don't remember exactly the date.

Q. Approximately ten years ago, would you say?

A. Approximately ten years ago.

Q. What kind of work did you do for them, what kind of plastering? On what kind of houses or units did you do it?

A. Oh, all single units, single houses.

Q. Was that on contract? A. Yes, it was.

Q. Are you familiar with the duplexes that Artcraft built and later deeded to its stockholders?

A. Yes, I am.

Q. Were you asked to bid on those jobs?

A. I was.

Q. Did you bid on them? A. No, I didn't.

Q. Why didn't you?

A. During the course of my conversation with Mr. Pool as to the type of work he was going to do on these houses, and the specifications of the work he had wanted to do there, I told him I asn't able to supply the amount of men necessary [132] for that length of time to do that job.

The Court: For that what?

The Witness: For that particular job.

The Court: At that particular time?

The Witness: That particular bunch of units they were going to build.

The Court: All right.

(Testimony of Thomas H. Block.)

Q. (By Mr. Axelrad): Why was the number of men an important problem?

Mr. Chehock: Pardon me. I don't know as the witness is clear. I know I am not clear on what he is talking about. What houses are you talking about?

The Witness: These duplexes and apartment houses.

Q. (By Mr. Axelrad): These are the 22 apartments and 70 duplexes back there in——

A. Yes, and the 100. Each time I was asked to bid.

Q. And each time did you refuse? A. Yes.

Q. Why did you refuse?

A. Because of the scarcity of men.

Q. You had bid on their other jobs, is that correct? A. That is right.

Q. And you had taken these jobs?

A. That is right. [133]

Q. What was there about these jobs that made the scarcity of men a problem?

A. May I explain? On ordinary homes and shacks, like we call them, there is a certain standard specification and quality of work we do. It isn't under the strict supervision that they usually get when a man is building houses for rent or for his own personal property or his use.

Q. Are you suggesting that the specifications for these duplexes and apartments were more stringent than normal?

A. That is exactly the reason I didn't do them.

(Testimony of Thomas H. Block.)

Q. Were they more stringent than had been customary with the Artcraft people on their individual houses that they were building for sale?

A. Yes.

Q. In what way?

A. They used different type material, and the type of work you had to do, it took longer to do it.

Q. What kind of materials were different?

A. Like they used a metal lath instead of plasterboard, to name one thing.

Q. Metal laths in the duplexes and apartments?

A. Yes.

Q. Was that customary on houses that were being built for resale? [134]

A. No, it was not.

The Court: I think you are assuming some things in your questions, and I don't want to have difficulty with this record when I start finding facts. You are implying that it is established here that these houses weren't being built for sale, and I think that is one of the things I am going to have to decide, for instance.

Your questions are carrying the implication there that I would rather you avoided. You let him answer the questions and leave out the implications. When you describe what the houses are and if they should be building these cheaper houses, it could be conceivable that people might be building those and not building for sale.

You just ask him the questions and let him give the information.

(Testimony of Thomas H. Block.)

Q. (By Mr. Axelrad): Mr. Block, you say that there was in the specifications for these three tracts expandable metal laths, is that correct?

A. That is correct.

Q. Was that a normal kind of specification for tract building? A. No, it was not.

Q. Had you been doing a lot of subcontracting on tract houses? [135]

A. That is all I did.

Q. For how many years?

A. I think I did the first house, plastered the first house that went in in Southern California.

Q. Did you ever find expandable metal laths in those kind of houses?

A. Only at one time during the war when plasterboard was not available and they were forced to use it, and then only until they were able to put plasterboard back.

Q. This was during the war?

A. This was during the war, during the war years around 1944, 1945.

Q. Was that the situation in 1943 and 1944?

A. No, it was not.

Q. There was plasterboard available for these tracts?

A. Yes, there was material available.

Q. And he still specified metal laths?

A. Yes.

Q. Do those take more man-power?

A. Yes. It takes at least half again as many

(Testimony of Thomas H. Block.)

man-hours as it would under normal conditions on both the lathing and the plasterboard.

Q. Did you have more jobs than you could take care of, more people requesting you to bid and do jobs?

A. At that time I was doing four other tracts' houses. [136]

Q. Was that pushing you as far as available man-power was concerned?

A. That is the main reason I couldn't do the job.

Q. Could you have done this job were it not for the differences in the ways they wanted it done?

A. I could have handled it fine.

Q. What else was different besides the metal lath about these specifications?

A. The quality of work in these tracts under normal circumstances. We all do pretty good work normally, but in this particular case he wanted everything rodded and straight-edged, the kind of a job that would take about twice as many man-hours to finish as it would to do a normal job.

Q. Was this customary with most tract builders, to do these additional things you are talking about?

A. No.

Q. It was not?

A. They looked for a good, clean job, but they didn't demand a straight-edge job.

Q. Did Artcraft Builders in the other houses you have built for resale——

The Court: That would be a better way to put it than the other way you put it.

(Testimony of Thomas H. Block.)

Q. (By Mr. Axelrad): ——did they have those [137] specifications in those particular houses?

A. No, they didn't. They were normal jobs.

Q. Did you have any discussion with them about these new kind of specifications? Did you ask them why, or did they volunteer, or did you find out why they wanted them?

Mr. Chehock: I object to that as hearsay.

Mr. Axelrad: It wouldn't be hearsay, your Honor.

The Court: Of course, it is hearsay.

Mr. Axelrad: Or I should say I am purposely asking him about it, because——

The Court: It isn't anything else but hearsay, but I think we might allow it to come in. Go ahead.

The Witness: When I was talking to Mr. Pool, I asked him why does he want to go to that added expense, putting in the expandable metal and doing that for rental units, when under normal circumstances rentals take an awful beating. I didn't know how long he was going to keep them, or what the purpose was. I thought it would be a lot cheaper if he built normally.

His answer was he was building them for his benefit, his private income, and he had no intention of selling them, he was going to use them for income only, and he wanted them well constructed so it would take the beating that rentals normally take. [138]

Q. (By Mr. Axelrad): Do you have any personal knowledge of whether other specifications were similarly stringent, those for any other build-

(Testimony of Thomas H. Block.)

ing trades? Did you have any discussion about that?

A. Yes. I noticed he had a good deal more tiling in it, and his carpentry work was different than the way we built our homes normally. His foundations were built larger. Just in general, he overbuilt those houses.

Q. Was it different than Artcraft had been doing in these respects with their other houses?

A. A good deal different.

Q. What was Artcraft's reputation as a speculative builder prior to the time those were built, do you know?

A. Their reputation, or what I heard of it, they were good pay and they were fine people to work for, and they built good homes.

Q. They weren't known as having built shoddy houses? A. That's right.

Q. So the effect of these more stringent specifications was not to produce merely a good house, but a better than average house? Would you say that is correct?

A. That is what I testified.

Q. We were speaking of plastering. Did you also, in your subcontracts, normally do the stucco [139] work on the outside? Is that included in the plastering contract? A. Yes, it is.

Q. Did they ask you to bid on the stucco on these particular tracts? A. Yes.

Q. Were the specifications concerning stucco any different than normal?

A. On these particular rental units they were

(Testimony of Thomas H. Block.)

different than the normal houses we built for them.

Q. In what particulars were they different?

A. Well, it is pretty hard to explain without going into a great deal of detail, but it took more nailing, more reinforcing. There were places where we would hang paper on the outside of the building with a few odd nails, which were sufficient to hold it until we got the wire around it, and then we renailed it every six inches on each stud. It is too lengthy a detail to explain, but it was a labor killer. The specifications just took half again as much time to do that type of work than normally.

Q. Were these additional things that were specified calculated to make the house look better so that it might sell better, or what do you suppose could be the purpose?

Mr. Chehock: I object to that, your Honor, as calling for a conclusion and opinion of the witness, and the witness is not properly qualified. It is immaterial. [140]

Mr. Axelrad: As far as the opinion of the witness, he has testified he has been a subcontractor in this field for 25 years, and I would think if anyone would know what makes one job better than another, it is this witness.

Mr. Chehock: He is also asking this witness indirectly to tell what was in the mind of the Pools and Murphys, which is hearsay.

The Court: I don't know that he would know necessarily. I think there is a lot to the objection. But you may answer by doing this: You may give

(Testimony of Thomas H. Block.)

your opinion as to what the effect of this different type of work would be as it has to do with the finished house.

The Witness: Well, sir, for the information of counsel, I hold a general contractor's license, also.

The Court: I am interested in your answer to the question, and not in what you want to say to him.

The Witness: All right, sir.

The Court: You just answer my question.

The Witness: It would make a nicer, better house.

The Court: He is not the one that is going to find the facts here. I am the one that will have to struggle with the evidence to find the facts.

The Witness: It would tend to make the job longer and better, make it stand up better over a longer period of time. Under normal precautions [141] taken there, with an ordinary tract house, when the builder builds them and sells them, he is gone and it doesn't make any difference.

The Court: That doesn't sound like he is building the job very well.

The Witness: It would surprise you what they do, what they get away with.

The Court: Go ahead.

Q. (By Mr. Axelrad): Would this kind of job in appearance be any different than any other plaster job? A. No, it wouldn't.

Q. It was not a matter of appearances at all, then? A. No, it was not the appearance.

(Testimony of Thomas H. Block.)

Q. Did Murphy or Pool, or both of them, tell you why they were building these?

Mr. Chehock: That is hearsay. I object to that as hearsay.

The Court: I think I will sustain the objection. He has already made his statement once. I think he has said as much as he could, so I will give that much weight to it. This would be repetition.

Mr. Axelrad: I think your Honor is correct. I did ask something of the same, but I was going to lead into something else.

The Court: Well, you get to it in some other way. [142]

Mr. Axelrad: All right.

Q. (By Mr. Axelrad): These particular tracts that we are talking about, the 100, the 70 and the 22, have you ever visited them since they were built? Do you know where they are?

A. Yes, I do.

Q. Did you ever go in any of them?

A. I was working in the immediate vicinity, all around there, and I went through them dozens of times.

Q. While they were being built?

A. While they were being built.

Q. Who was in charge or supervision of construction for Arteraft at the time, do you know?

A. Well, Mr. Pool.

Q. Did you have any occasion to learn from anybody what kind of supervision Mr. Pool was giving these particular jobs?

(Testimony of Thomas H. Block.)

A. From my personal observation, Mr. Pool was on the job constantly, all day long.

Q. Did he have usual standards or high standards or low standards about the kind of construction?

A. Mr. Pool is a good builder. He demanded good work.

Q. Do you have any knowledge about the time these tracts were offered for sale? Were you present at any discussions concerning whether they should be sold? Did you offer any advice? [143]

A. No. I wasn't there when they first started, but I had talked to Mr. Murphy several times, asking him why he hadn't sold those buildings with the rising market, and it looked like there would be a good chance. In fact, I advised him to sell and grab what I thought was some easy money at that particular time.

Q. In what capacity did you advise him? As an ex-subcontractor?

A. No, as a personal friend. I thought the market had reached its top, and the war being over at that particular time, I thought everything would drop down. It was just conversation. I thought personally it would be a good chance to move them.

Q. Do you know what month you are talking about or what year?

A. No. It was during the war.

Q. During the war?

A. Right after the war.

Q. Right after the war? A. Yes.

(Testimony of Thomas H. Block.)

Q. What did Murphy respond to those suggestions?

A. That he had no intentions of ever selling those houses.

Q. Did you ever talk to Pool about them? [144]

A. Practically the same identical thing, several times.

Q. When they were offered for sale, were you still working in that area?

A. Yes. I worked in that immediate area for about five or six years.

Q. Were you present when they were being advertised and when people were there, were you ever in the house?

A. I came by there one Sunday. In fact, I was on the way out to play golf and I saw a crowd of people around the office so I stopped to see what was going on.

Q. And what was going on?

A. I found they had advertised those units for sale and Mr. Boland and Mr. Smith were there, and I think there were 30 or 40 or 50 more people there.

The Court: Who is Smith?

The Witness: One of his salesmen.

Q. (By Mr. Axelrad): Whose salesman?

A. One of his salesmen, one of Mr. Boland's men that he had on that tract.

Q. You mean Mr. Smith worked for Mr. Boland? A. Yes.

Q. Who else was there?

A. Plenty. In what respect?

(Testimony of Thomas H. Block.)

Q. Who was in the office? You say you saw a crowd of people. [145]

A. They were total strangers to me.

Q. Total strangers? A. All strangers, yes.

Q. Where was Murphy? A. Murphy?

Q. Or was he there? A. No.

Q. Was Pool there? A. No.

Q. Do you know their regular employees?

A. I know them all well.

Q. Were any of them there?

A. No, they weren't.

Q. You say that you saw these duplexes after they were completed, and the apartments, is that correct? A. That is correct.

Q. What was their general appearance? Were they well kept up?

A. Yes. They were nice buildings.

Q. Were they well landscaped?

A. They had a nice job of landscaping around them, nice paint job, the streets were nice. In general, it looked like a nice tract of homes.

Q. Did you ever have any financial interest in Arteraft? A. No. [146]

Q. Or in any joint ventures with Murphy or Pool or their wives?

A. Never. The only thing I had to do with them financially was subcontracting the plastering.

Q. That was always a fixed contract?

A. Always at a fixed cost, yes.

Mr. Axelrad: That's all.

Mr. Chehock: With the Court's permission—I

(Testimony of Thomas H. Block.)

have over here a number of papers and notations —I would like to be seated while questioning the witness, if that is all right.

The Court: Go ahead.

Cross Examination

Q. (By Mr. Chehock): Mr. Block, when were the 70 duplexes built?

A. When were they built?

Q. Yes.

A. Well, everything I am going to say I am guessing. I am not quite sure of the exact date, but I think they were built around 1943, I think.

Q. When were the 100 duplexes built?

A. It seems to me they were built either in 1945 or 1944, late 1944, or *1955,* I think; may have been a little previous to that time. [147]

Q. When were the 22 apartments built?

A. They were built first, they were the first ones built. I think they were built in late 1942. I am also guessing now.

Q. Artcraft have the reputation of building quite good homes, is that not true?

A. That is correct.

Q. Is that not true, also, of the houses they built in 1942 and '43?

A. Yes, sir, they were nice homes.

Q. You don't mean to imply by your testimony, do you, Mr. Block, that different builders don't require different things for building homes, even though they are tract homes?

(Testimony of Thomas H. Block.)

A. I don't know how to read what you are trying to say, but I will say we all have a standard specification, which is the minimum of labor and materials to be used in these homes. They all try to get as good a job as possible, but they pay the least and they ask for the least that they can use to get by satisfactorily, to pass inspection.

Q. What I am trying to ask you, Mr. Block, is that a number of the builders, good builders, require good materials to go into their houses, don't they?

A. Yes, sir; all our materials are standard.

Q. Well, take this metal lathing you are talking about in the plastering. [148]

A. That is right.

Q. Aren't there other tract houses that were built about that time that had those in them?

A. The only time any builder in Southern California—and I am making this as a statement—ever used metal lath is because he couldn't get plasterboard to be used at that particular time. He didn't use it because he wanted to. He used it because he had to, and it was only a temporary deal.

Q. Is that the reason Mr. Murphy and Mr. Pool used it?

A. No, sir. There was plenty of material available for Mr. Murphy and Mr. Pool at that particular time.

Q. Do I understand your testimony is that there weren't others, then, that did use metal?

A. Not on tract homes, yes, sir.

(Testimony of Thomas H. Block.)

Q. You are testifying only as to your own knowledge, are you not?

A. I am testifying to the fact that, without being a braggart, I think I was doing as much plastering as any man in Southern California at that particular time. I bid on most of the tracts.

Q. That may be, but you wouldn't be handling all the tract houses in Southern California, and you don't mean to imply that.

A. No, but I bid most of them, whether I got [149] them or not. You don't get all you bid on.

The Court: How big an organization do you have?

The Witness: At that particular time, sir, I was carrying about 200 men.

The Court: What do you call Southern California?

The Witness: Well, I mean the biggest part of the building around Los Angeles proper, because there is where our first tract homes originated, right up around here.

The Court: By that, then, you mean Los Angeles?

The Witness: I mean around Los Angeles County.

The Court: All right.

Q. (By Mr. Chehock): When did you have these conversations with—or with whom did you have these conversations when you are talking about not wanting to sell and wanting to rent? With whom were those conversations?

(Testimony of Thomas H. Block.)

A. Both Mr. Pool and Mr. Murphy.

Q. Where were they?

A. On the jobs or in their office.

Q. Was it at the time you were making a bid?

A. One of the things is at the time we were making the bid, they told me that they were building those houses that way because they intended to keep them for income purposes.

Can I verify that a little bit? [150]

Q. I beg your pardon?

A. Can I verify that statement a little bit?

The Court: What do you mean by "verify"?

The Witness: Add a little to it?

Mr. Axelrad: Amplify it?

The Witness: Amplify it. I beg your pardon.

Q. (By Mr. Chehock): All right, go ahead.

A. I am sorry. I meant amplify it. At that particular time they were going to build a business block in that immediate vicinity, also, for income purposes, and they wanted their homes there so they would have all their interests in one corner.

Q. Sort of a development?

A. Sort of a development, yes.

Q. Do you remember the conversations you had with the builders on all your prospective jobs?

A. I don't have that type of specification to contend with with a normal builder.

Q. Does this metal lath have something to do with FHA requirements?

A. FHA does not require metal lath.

Mr. Chehock: I think that is all.

(Testimony of Thomas H. Block.)

Mr. Axelrad: Step down.

The Court: You are excused.

(Witness excused). [151]

Mr. Axelrad: I will ask Mr. Murphy to take the stand again. He was on cross examination.

Whereupon,

WILLIAM K. MURPHY

called as a witness for and on behalf of the Petitioners, having been previously duly sworn, resumed the stand and testified further as follows:

Cross Examination

Q. (By Mr. Chehock): Mr. Murphy, how long have you and Mr. Pool been the active heads of Artcraft?

A. Since approximately the middle of April or May 1943. Now, I say I am speaking of both of us. Mr. Pool was vice president and director prior to that time.

Q. From the time of organization?

A. Yes, sir.

Q. What was your capacity prior to the middle of 1943?

A. Well, I had charge of all the customers and laying out their plans for proposed contract building. I think I had the title of sales manager, if I had a title.

Q. Just carry on through from the beginning of Artcraft up to date as to what your offices were and what your duties were in Artcraft, what activities you had, would you, please?

(Testimony of William K. Murphy.)

A. Yes, sir. From the inception? [152]

Q. Yes, just generally.

A. Well, in April 1941, Artcraft was incorporated and Mr.—my position was running the office and taking care of applications to FHA and handling the people that were building on contract with, and securing the draws of the progressive payments from the bank as we progressed in the development of the different houses that we were building under contract. That was, generally speaking my work up until the time that we went to develop the first tract in Long Beach in May 1942.

Then I think down in Long Beach I took care of the time books. I handled all the contacts with the Federal Housing Administration, the banks, War Production Board, National Housing Authority, and helped out Mr. Pool generally in the payment to the subs, and things like that. That ran up till, I would say the middle of April 1943, or the middle of May; I am not sure which. I think one month there may be wrong one way or another.

Then I was made secretary and treasurer and a director of Artcraft. I had substantially the same work after that as I did before.

Q. Up to the present time, you mean?

A. Yes, sir.

Q. Now, tell us about Mr. Pool. Has your title been, from 1943 on, secretary and treasurer? [153]

A. Yes, sir.

Q. Have you been the sales manager?

(Testimony of William K. Murphy.)

A. No, I was not the sales manager after April or May 1943.

Q. You have already told us generally what your duties were? A. Yes.

Q. Now, Mr. Murphy, tell us about Mr. Pool.

A. Well, Mr. Pool, he supervised the layout of houses, and from the inception of Arteraft the contract purchasers or proposed purchasers would come in the office and go over the layout of the house that they would like to have built, and generally Mr. Pool used to break down the house, that is, the plaster, concrete, hardwood flooring, roofing, plumbing, and make an estimate on it and arrive at the price which they paid for the contract to build the house.

That ran up until we went down to Long Beach in 1942, in May. At that time he supervised the construction of the forms, that is, the concrete forms for the foundation, and the purchase of all the materials necessary to go in the first tract, which consisted, I think, of 143 houses.

In addition to that, he talked with the subs, and after the job got started, he supervised the construction. He would go out to the tract about 8:00 o'clock in the morning, and then I would see him [154] at noon, and I would see him again at 4:30, after lunch. Generally he was always on the tract supervising the work.

Q. The actual construction? A. Yes, sir.

Q. You didn't supervise that end of it?

A. No, sir.

(Testimony of William K. Murphy.)

Q. What other house-building activities did you or Mr. Pool have during any of these periods from 1941 to 1950, in other partnerships or other corporations, if any? A. Between 1941 and 1950?

Q. Yes.

A. We built a tract of 143 houses for sale.

Q. Just tell us in what organization it was?

A. Artcraft Builders, Inc., the company that is in question here.

Q. All right.

A. Then we built 100 houses for sale in Tract 12288 in Long Beach, this same corporation, and we built 87 houses for sale. That was all during the years 1942, from May, I think the 29th, until approximately July of 1943.

Then we built 22 apartment buildings that are in question here in 1943.

In 1944 we built 70 apartment buildings.

In 1945 we built 100 duplexes.

The Court: Were those 70 apartment buildings that you said? [155]

The Witness: Yes, sir, duplexes.

The Court: You said 22 apartment buildings. What is the difference?

The Witness: The 22, I distinguish it, some of those are two apartments, some of them have three apartments in them, and some of them have four apartments in them. There are 22 buildings.

The Court: All the others only had two, is that correct?

The Witness: That is correct, yes, sir.

(Testimony of William K. Murphy.)

The Court: All right.

The Witness: Then, in addition, we had filed applications to build, I think, one other tract, maybe two. I don't remember.

Then we built a market building which now houses the Alpha Beta Market, a drug store, and a shoe store.

Then we built the bank building, which houses I think it is seven business rentals.

That was all we built in this course.

Q. (By Mr. Chehock): Who is this man Durkin, or something like that? A. Who?

Q. Isn't there a man named Durkin or something like that, that one of you men were in partnership with? A. No. [156]

Q. Weren't one of you men in some partnership aside from Edward Pool & Associates?

A. Not that I remember.

Q. I don't seem to run across the name in my notes right here now. Maybe I will later.

Have you testified, then, as to all the building activities you men have been engaged in during this period 1941 to 1950?

A. Are you talking about this corporation?

Q. I am talking about any activities you men have been in.

A. In 1950 we formed a new corporation over in New Mexico.

Q. Tell us about that.

A. And started a building operation. That was in the fall of—I think it was built in 1951.

(Testimony of William K. Murphy.)

Q. What did you do there?

A. Built—Artcraft Builders, Inc., of New Mexico, built 98 houses.

Q. What kind of houses?

A. Single family.

Q. What did you do with them?

A. They sold them.

Q. You mean Artcraft sold them? [157]

A. Yes, sir.

Q. Did they turn those over to you, Murphy and Pool individually, and then did you sell them?

A. No, sir.

Q. They sold them directly? A. Yes, sir.

Q. Have there been any other building projects that you have been in?

A. The Artcraft Builders, Inc., of Colorado.

Q. Tell us about that, when that was organized and what they did.

A. That was organized in 1951. They built, I think it was 192 houses for sale.

Q. And were they sold?

A. Well, all of them—they are selling them, yes.

Q. They are what?

A. They are selling them.

Q. They are selling them now? A. Yes.

Q. Individual houses?

A. Single-family residences.

Q. They are sold by individual houses?

A. Yes, sir.

Q. That is true in New Mexico, also?

A. Yes, sir. [158]

(Testimony of William K. Murphy.)

Q. Are you and Mr. Pool the active heads of those two corporations?

A. Well, there are three partners, Mr. Pool, myself, and Major General Hurley.

Q. Hurley is in both of them? A. Yes, sir.

Q. Is it incorporated? A. Yes, sir.

Q. Then when you use the word "partners" you don't mean partners.

A. No. I am sorry. I mean three owners.

Q. What are your titles in those corporations?

A. Well, I am secretary and treasurer. Mr. Pool is president, that is, in the New Mexico corporation. And I am secretary-treasurer and Mr. Pool is president in the Colorado corporation.

Q. Did Mr. Pool supervise construction of both these projects? A. Yes, sir.

Q. What was your part in them?

A. Well, my part was the same as it was with Arteraft. I would handle the office, contact the Federal Housing Administration, secure the necessary financing. I never sold any of the houses, if that is what you mean.

Q. How did you dispose of those houses in New [159] Mexico? And how are you disposing of those in Colorado? A. Had brokers sell them.

Q. I believe you testified on direct examination something to the effect that you and Mr. Pool had some difference of opinion with Smith and Cooke as to the type of properties to be built by Arteraft, is that right?

A. Well, it was mostly Mr. Pool had it, but I

(Testimony of William K. Murphy.)

was agreeing with Mr. Pool, that is correct, yes, sir.

Q. As a result of those differences, what did you testify happened?

A. Well, I don't remember whether I testified as a result of them or not, but they didn't want to build apartment buildings, and we bought them out, bought their stock.

Q. When was that?

A. That was in May 1943.

Q. I think the stipulation of facts here shows, Mr. Murphy, that application was made with the FHA to build the multiple houses and the 70 duplexes prior to that time.

A. What is the date of the application?

Q. The date of the application on the 22 structures is of February 24, 1943, and the application on the 70 was on May 26, 1943.

A. Well, the 70 was, I think, after they decided to sell out. The 22 was before they sold out. The fact of the matter is, that is what brought it to a head. [160]

Q. They had a vote there, didn't they?

A. They had a vote, but I would file the application and it was my job to handle it and see that it went through FHA, so I filed the application and sent it in.

Q. Without their approving it?

A. I don't know whether they approved it or not. I don't remember. Mr. Pool did. They were never active. They were never on the job, I mean.

(Testimony of William K. Murphy.)

The only time they would show up would be at the directors' meetings.

Q. Then you and Mr. Pool have been the active heads of Artcraft from the beginning?

A. I wouldn't say I was. I was not an officer.

Q. You were from 1943 on, and he was from the beginning. A. That is right.

Q. In the years 1943 and 1944, along about the time these 70 duplexes and later these 100 duplexes were built, there was a scarcity of materials, wasn't there, and that is the reason why priorities had to be received first?

A. Well, there was a scarcity of materials and priorities. They would not allow you to build anything that was not helping the war effort. That is why the priorities.

Q. About that time they——

The Court: Well, that was controlling materials as part of that picture, wasn't it? [161]

The Witness: Yes, sir, absolutely.

The Court: All right, then.

Q. (By Mr. Chehock): At about that time in 1943 and 1944 and 1945, along there, the NHA granted priorities only to those that would build multiple houses, isn't that right?

A. Not to my recollection, no, sir.

Q. Wasn't there a period in 1943 when NHA wouldn't grant priorities on singles, but would on duplexes?

A. Not that I know of. They were building single-family residences all the time we were build-

(Testimony of William K. Murphy.)

ing our multiple units, right across the street from us, and I was pretty familiar with the NHA regulations.

Q. What were the regulations, the Government regulations?

At that time they required the 70 and 100 to be rented to eligible war workers, isn't that right?

A. Yes, sir.

Q. Did that include veterans?

A. It did in our case.

The Court: By "veterans," I think maybe we better clear that up, if there is any problem. I don't know whether there is or not. In some respects the word "veteran" is generally applied to people who have been in the Service and are out. Where that is done, usually the reference to those that [162] are still in is men in the Armed Forces.

When you say that these structures in 1943 and 1945, that you restricted the sale to war workers and included veterans, are you talking about men who have been in the Service and are out, or are you talking about the Armed Services, or just what?

The Witness: I did not mean veterans. I don't know whether Mr. Chehock did or not.

The Court: I was wondering. I was afraid we might have something here where we did not know what was meant.

The Witness: No, sir.

The Court: So to clear it up, what did you mean?

(Testimony of William K. Murphy.)

The Witness: I meant people in the Armed Services and migrant workers.

Q. (By Mr. Chehock): Can you give the Court just a general description of where these 70 duplexes and these 100 duplexes were in relation to each other, and also in relation to the Douglas plant and any other defense projects in that vicinity?

A. They were approximately, the 70 duplexes were approximately two miles and a quarter south of the Douglas plant, and the 100 were, I would say, two miles and three-eighths. They were nearby.

The other defense plants, the closest one I know [163] of was the California Shipyards, approximately 13 or 14 miles.

The Court: That was over here in San Pedro?

The Witness: Yes, sir. Or in Wilmington.

The Court: Wilmington?

The Witness: Yes, sir.

Q. (By Mr. Chehock): I think we all know, but so the record can show, what was the Douglas plant?

A. The Douglas plant, they manufactured airplanes.

Q. How big a plant was it?

A. Well, they ran three shifts. I don't know. I imagine they had thousands of employees, twenty-five or thirty thousand. Maybe more than that. I don't know.

Q. Were these 70 and these 100 houses the closest tract houses to the Douglas plant?

(Testimony of William K. Murphy.)

A. No, sir.

Q. Were there several tracts there?

A. Yes, sir.

Q. You say they were about two miles away?

A. I would say two and a quarter, two and three-eighths miles from the plant.

Q. Where were the 70 duplexes in relation to the 100 duplexes?

A. Well, they were a little west and south of them. [164]

Q. How far apart?

A. Oh, not over one-eighth of a mile. Well, maybe a little more than that to the end of the tract; a half a mile, quarter of a mile, something like that.

Q. Well, what would the closest point be, approximately?

A. About a couple of blocks, I would say, maybe a block and a half. I am not positive.

Q. Was this undeveloped land when Arteraft acquired it? A. Yes, sir.

Q. What kind of land was it?

A. Well, just raw acreage.

Q. What did Arteraft do with the land after they acquired it? A. They subdivided it.

Q. Arteraft made application and obtained the FHA loans? A. Yes, sir.

Q. And you are the one that took care of that end of it? A. Yes, sir.

Q. Then Arteraft built the 70 and 100 duplexes?

A. Yes, sir.

(Testimony of William K. Murphy.)

Q. On the 100 duplexes, Artcraft collected the rent on those until February 1, 1946, is that not right? A. Yes, sir. [165]

Q. And reported that rent in the corporation return? A. Yes, sir.

The Court: Does the record show when these rents started, the extent, and so forth?

Mr. Axelrad: The stipulation shows almost all of these things.

The Court: All right. I rather judged it did, but we have been covering a whole lot of stuff all day that the stipulation shows. All right, go ahead.

Q. (By Mr. Chehock): Mr. Murphy, I believe you testified in direct examination something to the effect that multiple houses were better income-producing houses than single houses, is that not true? A. That is a fact, yes, sir.

Q. And the more units there are in a particular house, the better it is from an income standpoint, is that right? A. Yes, sir.

The Court: When you can get a tenant?

The Witness: I mean that, yes.

Q. (By Mr. Chehock): When were the 22 built?

A. The 22 were built, started in August, I think, 1943.

Q. When were they completed? [166]

A. We rented the first one the day before Thanksgiving, 1943. I would say they were completed approximately in December 1943.

Q. When were the 70 built?

A. I think the 70 were started in the fall of

(Testimony of William K. Murphy.)

1943 and completed, perhaps, in April or May, along in there, in 1944.

Q. When were the 100 built?

A. They were finished in 1945.

Q. Tell us about when they were started and when they were finished.

A. When I say started I am talking about putting a spade in the ground, and they were started months before that, all the preliminary talks that you have to go through before you can start.

Q. You just tell us what you want to tell us, but tell us when they were started.

A. The preliminary applications on the 100 were filed sometime in, I would say, October 1944.

The Court: When did you put the spade in the ground out there?

The Witness: I would say in February 1945.

Q. (By Mr. Chehock): When were they completed? A. Around July 1945. [167]

Q. Were all 100 completed then? Don't your minutes of February 1, 1946 state something, now that they are completed, something about transferring them over to you?

A. I don't recall what the minutes state. The buildings were completed and we had people moving in there in May 1945.

Q. Are you sure all 100 were completed that early in 1945? A. I am positive of it.

Q. When would you say they were completed, then?

(Testimony of William K. Murphy.)

A. I would say not later than the 15th of August.

Q. Of 1945? A. Yes, sir.

Q. And the ceiling on the selling of these tract houses was lifted in October 1945, is that right?

A. Are you talking about the apartment buildings?

A. I am talking about the duplexes, the 100 and the 70.

A. I don't know whether it was or not.

Mr. Axelrad: What ceiling are you talking about?

Mr. Chehock: The selling prices on these duplexes.

Mr. Axelrad: It doesn't appear that there was a selling price.

Q. (By Mr. Chehock): The Government ceiling on the selling price of houses was lifted in October 1945, isn't that right? [168]

A. I don't know. I never inquired.

Q. Wasn't it during this period you say that the houses went up in value, and wasn't that as a result of the ceiling for the selling price of the houses being taken off of them, wasn't that the reason they did go up?

A. Your houses doubled in value there in two months along in May, the latter part of April, 1946. There was no appreciable raise in the cost of construction in August 1945.

Mr. Axelrad: Your Honor, I would like to interrupt at this point. I think the way the question

(Testimony of William K. Murphy.)

was asked, it leaves a misleading conclusion or possible inference in the record. There was never any ceiling price on houses as far as OPA was concerned. The resale price of used houses was never subject to rent control.

The Court: That would be a question of what the regulations and restrictions showed.

Mr. Axelrad: He talked about one being lifted that never was in.

The Court: I wouldn't be any more willing to take your statement that there wasn't any than I would the implication from the question, if there is such an implication, that there was.

The question has been asked the witness on cross examination here, and the witness said if there was, he didn't know anything about it. [169]

Further, I think that there is a whole lot of concern over something that is not to be concerned about at this time. If it does become pertinent to establish the record on it, you can do it by citation of the regulations and so forth, or if there wasn't any, that can be done at the proper time and in an orderly manner.

Mr. Chehock: I thought it was general knowledge, and if you refer to Order No. 601, which is Exhibit H-8-C, there is an NHA provision there that the sale price, except as provided in Section 4 hereof, is not in excess of the fair market value thereof or $6,000.00, whichever is lower.

I thought it was common knowledge and that this

(Testimony of William K. Murphy.)

witness would know that there was a lifting of the ceiling prices on these places in October 1945.

The Court: I would say if there is such a document as that as an exhibit to this stipulation, I don't know what it is, except the reference that has been made there, it is a proper subject of examination of this witness, and if he knows or he doesn't know, it is up to him to say so. After all, this is cross examination.

The Witness: These buildings cost us more than $6,000.00 to build. We never asked for a sale price on them. You will find you have to go through NHA to get the sale price, if you read further.

The Court: Which exhibit is that you are referring to? [170]

Mr. Chehock: H-8-C.

The Court: All right, go ahead.

Q. (By Mr. Chehock): Mr. Murphy, if the more multiple units there were in a particular apartment building, the more productive it was from an income standpoint, and since the 22 were applied for and built first, how come you reverted to just duplexes? Why didn't you go into more multiple houses?

A. For the simple reason that the land wouldn't divide up into large enough lots to put over two units on it.

The Court: What do you mean by "wouldn't divide up"?

The Witness: Where we built the 22 buildings was approximately ten acres or something like that.

(Testimony of William K. Murphy.)

The Court: You could have divided it up into small units or you could treat it as one unit, couldn't you?

The Witness: We were putting all the units on one floor, your Honor. We were not putting them two stories.

The Court: In other words, for what you wanted to do it didn't divide up.

The Witness: That is right.

The Court: All right.

The Witness: The 22 lots divided up into lots that some of them were 210 feet deep. In other [171] words, it was an irregular shaped piece of property.

Q. (By Mr. Chehock): All the projects that Artcraft built, this 142 built in 1942 and the ones built in 1943, the 70, the 22 and the 100 we have been talking about, were all Title 6 FHA loans?

A. No. The Title 6 FHA issued the insurance. They were private loans.

Q. But they were FHA-insured loans, Title 6.

A. The loans were insured by FHA, that is right.

Q. And they were Title 6 loans? A. Yes.

Q. Can you identify this here?

A. That is a print of the tract on which the 100 buildings, the duplexes were built.

Mr. Chehock: The Respondent offers in evidence the exhibit the witness has just identified as Exhibit UU.

The Court: Any objection?

(Testimony of William K. Murphy.)

Mr. Axelrad: No objection.

The Court: It may be so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit UU.)

Q. (By Mr. Chehock): Did you make a written contract with Mr. Boland?

A. I don't remember whether I did or not. I [172] know this: I have looked all through the files for it. Mr. Axelrad asked me to get it, if I had one, and I have been unable to find one. Still I have a recollection of something in writing, him writing us a letter or we answering it, but Mr. Lampe, our auditor, took a lot of papers from our office back in 1949 for one of the Internal Revenue men, agents, to go over down in his office, and we have never received them back since.

Q. Did you get after Mr. Lampe about it?

A. I intend to do that tonight. I think that is where the minute book is, too.

The Court: It seems to me like that would have been the first thing to do, to go to Mr. Lampe, when you were preparing for this case.

Mr. Axelrad: Mr. Lampe will be a witness here. He has been cooperating in the preparations. I have gone over that very carefully with him and he hasn't got it, he says.

The Court: All right.

Q. (By Mr. Chehock): Mr. Murphy, you have a number of leases in your possession covering the 22 apartments and the 70 and the 100. I have looked

(Testimony of William K. Murphy.)

them over and I believe that as far as the 70 and 100 are concerned, at least,—I am not sure about the 20—I think it is true all you have in your [173] possession are one-year leases, is that not true?

A. I don't know. It is a year, at least, I am positive of that.

Q. On the 70 and the 100?

A. At least that, yes.

Q. If you have any leases on the 70 and the 100 for a period greater than a year, would you produce them?

A. I would be glad to, yes, sir.

Q. I think they are all for one year.

A. They may be. I am not positive.

Q. Now, around March, you quit making written leases on the 70 and the 100 duplexes, didn't you, March of 1946?

A. No. I found one lease up there, I just happened to notice it, that was made the latter part of April.

Q. The latter part of April? A. Yes, 1946.

Q. Could you produce that?

A. Yes; I think it is in court here.

Mr. Axelrad: We tried to put it in evidence this morning. We will make that tabulation. A lot of these, counsel, are after that date.

Mr. Chehock: My recollection is, from looking over the leases you have on the 70, there is no lease after March 15, 1946, and on the 100 there is no lease after April 10, 1946. [174]

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MAR 15 1958
JOHN T. FEY, Clerk

# United States
# Court of Appeals
## for the Ninth Circuit

EDWARD POOL and LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY and EDNA MURPHY,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

# Transcript of Record

In Two Volumes

VOLUME II.

(Pages 259 to 535, inclusive)

Petitions to Review Decisions of the Tax Court of the United States

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Phillips & Van Orden Co., 870 Brannan Street, San Francisco, Calif.—2-18-57

# No. 15399

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(Testimony of William K. Murphy.)

Q. (By Mr. Chehock): Would that be right?

A. That is possible. It may be no lease expired.

Q. Isn't that true, around March or the first part of April, in that period sometime is the time you stopped taking written leases?

A. No, I wouldn't say that. I mean I am not saying that you are not right, but I don't know just exactly when we stopped taking them. We stopped taking them when our attorney told us that there was no benefit in having a lease.

Q. When did you have that conversation with your attorney?

A. Well, it seemed to me like it was in the spring of 1946.

Q. That would be around March or the first part of April, wouldn't it?

A. It would be around there sometime, yes, sir.

Q. After that time, March or April, whenever this conversation was with your attorney, as vacancies occurred in the 70 and the 100 duplexes, did you rent them or leave them vacant so that buyers could have something to move into? A. No.

Q. What was the situation?

A. We rented them. We had not decided to sell any property in March or April of 1946. [175]

Q. Did you rent them on a month-to-month proposition without a written lease?

A. I would say 99 per cent of them were leased.

Q. You stopped making leases after you had this conversation, written leases? You stopped mak-

(Testimony of William K. Murphy.)

ing written leases after you had this conversation with your attorney? A. That is right.

Q. Around March or April 1946?

A. That is right.

Q. As the units became vacant after that time, how did you handle it, what did you do?

A. Well, that would be on a month-to-month basis, if any vacancies occurred.

Q. From your records here, it shows that when these 100 were sold there were, I think, 130 of the units upon which there were no written leases of the 200 units. Does that sound to you approximately correct?

Mr. Axelrad: I object.

The Witness: No, it does not. Absolutely incorrect.

Mr. Axelrad: I object to anything, your Honor, about the records showing. The records do not show that. I don't think he ought to premise a question on a mistaken assumption.

The Court: Well, I don't know that there is [176] anything wrong with the question being on cross examination, but it hasn't elicited any information that would be of any moment, anyhow, so let's get along.

Q. (By Mr. Chehock): I noticed in looking over the files here that there are printed deeds made out for both the 70 duplexes and the 100 duplexes, the tracts, bearing the name of the four of you and bearing the name of the tracts, printed deeds. When were these deeds printed, do you know?

(Testimony of William K. Murphy.)

A. I don't know. I think the 100—the 70 were printed sometime the latter part of May or June 1946.

Q. Which were? A. The 70.

Q. Were they printed at the same time?

A. No, sir.

Q. They seem to be identical in all respects. Do you know who printed them?

A. No, I don't know who printed them.

Q. Do you know who ordered them printed?

A. Yes, I think Mr. Boland did.

Q. Who is this Ruby J. Woodruff who is mentioned in the deeds?

A. She is vice president. She worked for us for ten years as a bookkeeper.

Q. She will be a witness here, is that right?

A. Yes, sir.

Q. You said "for us." She has been the bookkeeper for whom, now?

A. Artcraft Builders, Inc.

Q. And for Edward Pool & Associates?

A. She kept our books also, yes, sir; that is, the corporation kept our books, so we will have the record straight. We didn't keep them.

Q. Why was the decision made to sell the 70 duplexes prior to the 100 duplexes?

A. No particular reason that I know of.

Q. Well, when was the decision made to sell the 70 rather than the 100?

A. Well, there was never a decision made to sell the 100, as I remember, until August 1946.

(Testimony of William K. Murphy.)

Q. I believe you testified on direct examination several had advised you that the prices had gone up considerably there in the—I think you will find that the ceiling on the selling price was taken off in October 1945, and although you didn't say that, the selling price started going up there, the fair market value was rising, is that right, for a period there at the end of 1945 and early 1946?

A. If you want my opinion, my opinion is that the prices hadn't gone up appreciably in 1945 at all. It was when the servicemen started coming back [178] and looking for homes, I would say in the latter part of February, March and April and May, and it really hit the top in September, August, along the latter part of 1946, and 1947, that is really when it hit. However, that is merely my opinion.

Q. On direct examination you testified that several of them talked to you and told you you should sell the 70, didn't you?

A. I testified that the resident partner of Arthur Young & Company, and Mr. Lampe.

Q. What are the factors that were considered by you or by your advisers on why you should sell the 70? Name all of them.

A. I can't name what they were considering.

Q. Name all you were considering.

A. I can name what they told me. They told Mr. Pool and I that the price had—the value of the property was so high, with rent controls on and the rent couldn't be increased, that it would be advis-

(Testimony of William K. Murphy.)

able to sell them, that an investment could be made better than we had there.

Q. Well now, is there any other factor that you considered as to why you should sell the 70?

A. Well, we were paying for counsel and guided by what they told us. We had no intention ever to sell them.

Q. Are there any other factors that you considered? A. I don't remember. [179]

Q. The reasons that you give here for selling the 70 were also equally applicable to the 100, weren't they?

A. Yes. The price on the 100 had gone up $1,000.00 or $1,500.00 in the meantime. The same applied to both of them.

Q. So there really was no reason for putting the 70 on any more than the 100, was there?

A. Oh, yes.

Q. I asked you what all the different factors were, and I thought you told me that was all. What else is there?

A. You are talking about the 100. We told Mr. Boland we didn't want to sell the 100.

Q. Why did you not want to sell the 100 and why did you want to sell the 70?

A. We didn't want to sell the 100 because we wanted to keep them for income, for an investment.

Q. The reason you sold the 70 is because the value had gone up and they told you you could make some money on them? A. Yes.

(Testimony of William K. Murphy.)

Q. Why isn't that also true of the 100?

A. I bought lots of stock and bonds, and when I liquidate a capital gain I don't usually sell it all necessarily. I might sell one-third and hold onto two-thirds or I may sell one-half and hold onto the other half. [180]

There was nothing motivating us to say we would sell the 70 duplexes other than the advice we had from what we thought was competent counsel, and at the time we were motivated to sell them we told Mr. Boland we didn't want to sell the 100 or the 22, and we never intended to. In fact, we told him that about the 70 on numerous occasions.

Q. With regard to the 100 and this advice you received—what is Mr. Lampe's capacity?

A. He is a certified public accountant.

Q. He makes your tax returns? A. Yes.

Q. Did you receive tax advice from him?

A. We received tax advice — well, I wouldn't know whether it was tax advice. We received tax advice from—I can't think of the gentleman's name. I can get it for you so you will have it tomorrow. He is a resident partner of Arthur Young & Company, and has a Scotch name.

Q. McTavish, is that the name?

A. That's it, yes.

Q. What did McTavish tell you?

A. McTavish said in his opinion the price of the buildings had gone up so much that with rent controls on it ceased to be a good investment, that we wouldn't be able to raise the rents until they

(Testimony of William K. Murphy.)

took off rent control, and he suggested we sell them. [181]

Q. The 70 and the 100? A. No, the 70.

Q. Wasn't that equally good advice for the 100?

A. We weren't discussing the 100.

Q. But wouldn't that be equally applicable to the 100?

A. I don't know. We didn't discuss it with him.

Q. You are and were then acquainted with the difference between long term and short term capital gain, weren't you, and the holding period of six months? A. No, sir, I don't think I was.

Q. Did you receive any tax advice in regard to the holding of these 100 for six months before sale?

A. Yes, sir.

Q. With whom did you discuss that? From whom did you receive the advice, and what was said?

A. Mr. Boland said that he could sell our apartments for double what they cost us, and that he had gone down on his own—incidentally, we didn't ask him to; never knew he went down, that he went down to the Internal Revenue Department in Los Angeles and laid the case of the 70 duplexes before the Internal Revenue Department. He said that he had been advised it was a long-term capital gain.

That was the tax advice we had, if you want to call it tax advice.

The Court: He told you that? [182]

The Witness: Yes, sir.

The Court: That they had told him that?

(Testimony of William K. Murphy.)

The Witness: Yes, sir.

Q. (By Mr. Chehock): Mr. Boland is going to testify here, is he? A. Yes, sir.

The Court: It sounds like a very strange story to me, because I never heard of the Internal Revenue ever giving out information on anything that approached a ruling or suggestion of a ruling under such a summary and extemporaneous manner.

The Witness: I am just explaining, your Honor, what was told me.

The Court: I understand you are saying what Mr. Boland told you.

The Witness: Yes, sir.

The Court: That would be an interesting story, I think. All right.

Q. (By Mr. Chehock): Did you consult Mr. Lampe about that or anyone else?

A. No, I don't recall talking to Lampe about it.

Q. Did you talk to some tax counselor about it?

A. No, not that I remember. I only talked to McTavish once, and Lampe, he was our auditor, [183] so that our—you know, our income taxes—but other than that, I——

Q. This 70 and 100 duplexes were sold under the name of Artcraft and were represented to the public as Artcraft houses being sold, weren't they?

A. I don't know how they were represented. I imagine the purchasers were told that Pool and Murphy owned them. I wasn't there when they were representing them.

Q. Well, all the ads carry—maybe not all of

(Testimony of William K. Murphy.)

them, but quite a number of them, that the builder is selling them, and most of the correspondence with the prospective buyers, and so forth, was under the name of Artcraft, is that not true?

A. No, that is not true.

Q. What is true?

A. It was not with Artcraft. That is not true. I don't know what is true. As I said before, I had nothing to do with selling the houses, and neither did Artcraft.

Q. Well now, you were the active head of Artcraft, weren't you? A. That is correct.

Q. As a matter of fact, didn't you have some conversation with your real estate man or others stating that by virtue of the good reputation Artcraft had in building houses, that would be of some sales advantage to use the name "Artcraft" in advertising these for sale?

A. So I won't be talking about a different thing [184] than you are asking me as to, I understood you to ask me, Mr. Chehock, didn't the public, the people buying these houses, think Artcraft was selling the houses. I answered you that I did not think so. They must have been told that Pool and Murphy were the ones that owned the houses, that Artcraft didn't own them. Now, they used Artcraft's name in advertising, if that is what you mean.

Q. Just elaborate on that.

A. Well, what do you want?

Q. Why did they use Artcraft's name in advertising?

(Testimony of William K. Murphy.)

A. I imagine Mr. Boland figured he could sell them easier if they knew Arteraft built them. We may have had, Arteraft had a pretty good reputation in the building business, and that is why he used the name of Arteraft in the advertising of them, but he had no authority to say the builder was selling them. In fact, I never saw that. Of coure, I wouldn't say what ads—I didn't see all of the ads, and it may be in there.

Q. Neither you nor Mr. Pool assumed any of the FHA mortgages that were taken on these projects, did you, the 70, the 22 and 100? Arteraft made the FHA loans and you did not assume the obligation, isn't that true?

A. My recollection is that we had to guarantee the Western Federal that the buildings would be completed individually. I am not positive, but I think that is correct. [185]

I think on the FHA commitment, in their opinion, the company didn't have enough money to finish the buildings. I think that is on all their commitments.

Q. What does that mean?

A. That means the corporation, to build 100 duplexes or 70 duplexes, didn't have the necessary money to build them.

Q. The 70 and the 100 were actually built for an amount less than the FHA loans, is that right?

A. That is correct.

Q. What do you mean, they didn't have enough money to build them?

(Testimony of William K. Murphy.)

A. I am just stating what was on the FHA commitment, what the Federal Housing Administration thought.

Q. I think the minutes of the corporation specifically show that you took these properties over specifically, and specifically stated that you do not personally assume the obligations.

A. That is correct.

Q. You didn't, then, assume the obligations of these FHA loans, did you?

A. I didn't say I did, no.

The Court: Well, you didn't say you didn't, and that is what he was trying to find out.

The Witness: I said before they started, your Honor, is what I meant to convey to him, I thought, [186] Mr. Pool and I guaranteed the completion of the buildings for Arteraft personally.

The Court: But he was asking you something else, which you hadn't answered.

The Witness: No, we didn't assume the loan.

Q. (By Mr. Chehock): You received cash for all the 70 and 100 duplexes that were sold, didn't you, in toto?

A. I think so, yes, sir. I am pretty sure.

Mr. Chehock: I might state to the Court that Petitioners' counsel and I have come to an agreement it will not be necessary to bring in the original newspapers and have them identified, and he is willing to waive identification; is that correct?

Mr. Axelrad: Yes, I am, your Honor, but I do object to the introduction of these things on the

(Testimony of William K. Murphy.)

grounds that they are irrelevant to any issue in this case.

The Court: I don't know what they are.

Mr. Chehock: I am not offering them yet.

Mr. Axelrad: I just wanted to make it clear that I was not agreeing to them as exhibits, although I agree to their authenticity.

Q. (By Mr. Chehock): I hand you an ad that appears in the Los Angeles Herald-Express of May 4, 1946, under the name of Artcraft Builders, Inc., [187] "For sale, 10 duplexes, by the builders." Do you know anything about that ad? A. No, sir.

Q. You will notice also the price is $11,800.00.

A. Yes, sir.

Q. That has reference to part of the 70, isn't that right? A. That is correct.

Q. I think the record here shows very clearly that those duplexes did sell for $11,800.00 rather than $10,800.00. A. That is correct.

Q. Where did you get this $540.00 figure you had in mind with Boland? Where did you get that figure?

A. I was multiplying five per cent of $10,800.00.

Q. You seemed to be quite definite that that arrangement would be five per cent and $540.00, but since he was using your office, it would be $500.00 and not $540.00. Now, was it $540.00 or some other figure? A. It was $500.00.

Q. What was the amount he agreed to take off by virtue of using your office?

A. He agreed to take five per cent and he would

(Testimony of William K. Murphy.)

allow us the difference between the five per cent and the $500.00. I thought the price was $10,800.00. So that would make it $40.00. [188]

The Court: Didn't you testify this morning about some representation, and so forth, of his to sell the properties for $12,000.00?

The Witness: Yes, sir.

The Court: Then in that case five per cent would have been $600.00.

The Witness: Well, the agreement was, your Honor, he was to get $500.00 and we were to allow him the office. That is what he was to get out of it.

The Court: I understand, but there was much said about $40.00 here this morning, and I was just interested, because if they had sold for $12,000.00, then the difference between $500.00 and five per cent was $100.00.

The Witness: Some of them sold for $12,250.00 and some of them sold for $13,000.00, but it still stayed at $500.00.

Q. (By Mr. Chehock): Which are you talking about now? A. The duplexes.

Q. The 70?

A. The 70. It was $12,250.00, the corners was.

Mr. Chehock: I think it is $12,200.00, isn't it?

Mr. Axelrad: Yes, it is $12,200.00.

Mr. Chehock: All right.

Mr. Axelrad: That has all been stipulated. [189]

The Court: We hadn't had any testimony about the matter stipulated, but we could have finished here, I think, with what we have had so far in

(Testimony of William K. Murphy.)

evidence in half the time, because I think a goodly part of what we are going over is matter that is stipulated. I don't say that critically, because sometimes it is necessary to state something that is stipulated in order to get the question and the answer on something that is not stipulated, but I don't think, since we have had all that on discussion, that we need every so often for the record to show all this is stipulated.

Let's get along with the cross examination. [190]

Q. (By Mr. Chehock): You will notice, Mr. Murphy, that that advertisement in there carries the name only of Artcraft Builders, Inc. and doesn't carry your name or Mr. Pool's name, and also it is advertising for sale "10 duplexes by the builders, immediate possession."

Isn't that a representation to the public that Artcraft is selling the duplexes?

Mr. Axelrad: I object, your Honor, on the ground that he is asking for a legal conclusion about what this constitutes as a matter of law. He has testified that he didn't know anything about these items.

The Court: I think it would be not a question of legal conclusion. It would be a question of fact, whether or not that on its face indicated a representation. This is cross examination.

Mr. Axelrad: I understand.

The Court: We have had much testimony here on direct which has tended to have been directed to the process that these people and Artcraft had nothing to do with the selling.

(Testimony of William K. Murphy.)

Mr. Axelrad: That is correct.

The Court: And this is rebuttal and cross examination, and it has to do with those same properties and representations that were made to the public [191] with respect to those properties, so it is perfectly fitting and proper.

Mr. Axelrad: Your Honor, isn't the issue who made the representation?

The Court: All right.

Mr. Axelrad: We don't deny that that was——

The Court: You are seeking to establish it. The government is complaining. Now we are getting the evidence that bears on it. So I am certainly not going to cut off—just because you have had oral testimony to the effect that it was one way, I am not going to cut the other party off from things that did transpire in connection with the sale of those properties, whoever did it, that might tend to indicate something else.

Mr. Axelrad: I am not trying to suppress any facts that are relevant here.

The Court: This is relevant and it is material. Now, it is a question as to whether or not it is true. It might be, and if there is a contradiction as to what is correct, then I will have to determine it, and I can't determine it if I have shut off the full picture. So you are trying to superimpose your presentation here on me in my province and my job that I have to do, namely, that of judging what the facts are when the evidence is in. This is part

(Testimony of William K. Murphy.)

of the presentation of evidence, and let's get along with it.

Mr. Axelrad: Your Honor, I would like to note an exception to your ruling.

The Court: All right. Let the record show an exception.

Mr. Axelrad: Because anybody can take an ad in the paper. I think that is common knowledge.

The Court: You are arguing as to whether it has some weight.

Mr. Axelrad: Right.

The Court: It is pertinent, it is material. It may not have any weight, because I may draw the conclusion that it is not so, but that is something that I am going to have to do. I am going to have to do it on the basis of the evidence, and not because I get part of the story in and the other is excluded.

Now, somebody apparently put such an ad in the paper, and it had to do with those properties and it had to do with the sale of them. All right.

Q. (By Mr. Chehock): Mr. Murphy, getting back to this ad here, is that a representation to the public that Artcraft is selling these properties?

A. Well, Artcraft Builders, Inc., is in the ad there, Long Beach, and it says, "For sale 10 duplexes by the builders."

The Court: I think that will speak for itself, [193] Mr. Chehock.

Mr. Axelrad: All right.

The Court: As to what the representation is.

(Testimony of William K. Murphy.)

Mr. Chehock: All right.

The Court: If it becomes material as to what the conclusion of the representation is, I will have to describe it.

Q. (By Mr. Chehock): In regard to these particular 70 and 100 being duplexes, rather than single-family units, actually, the fact that they were duplexes was a sales advantage, wasn't it, rather than a detriment?

A. I would say it was a disadvantage.

Q. Why would you say it was a disadvantage?

A. It is a lot easier to sell a single-family residence than it is a duplex.

Q. Did you have any trouble selling these 70 or 100? A. I didn't sell them.

Q. Did anybody have any trouble selling them?

A. I don't think Mr. Boland did, no.

Q. Isn't the fact that one of the units is income producing a sales advantage?

A. No, not in my opinion.

The Court: It could be. It might be under some circumstances and it might not be under others. I don't [194] think you can have a categorical statement one way or the other that would be true in all instances.

We will take an intermission.

(Short recess taken.)

Q. (By Mr. Chehock): Now, in regard to the entering into of one-year leases on these 70 and 100 duplexes, the entering into of those leases actually

(Testimony of William K. Murphy.)

was just as much an advantage from a selling standpoint as not having the leases, wasn't it?

A. No, I would say it was not.

Q. Why?

A. Well, if I was going to buy a duplex and wanted to live in one side of it, I would sooner it be empty.

The Court: You mean when you bought it?

The Witness: If I wanted to live in it, yes, sir.

The Court: By that you meant that if you bought the duplex and were going to live in one side, you didn't mean you would keep the other one vacant, but you would want it vacant when you bought it and you moved in, is that it? Or if you bought the duplex, would you keep the other side vacant?

The Witness: No. If I were going to move in, I would sooner have one side without a lease or vacant.

The Court: With no tenant?

The Witness: With no tenant. [195]

The Court: At any time?

The Witness: That is if I intended to move into it when I bought it.

Q. (By Mr. Chehock): What about the other one?

A. I would keep the other one rented.

Mr. Axelrad: He means one side, your Honor, I think.

The Witness: One apartment.

The Court: I understand, but it didn't make sense with the other answer. Of course, just for the part you would live in, even under rent control,

(Testimony of William K. Murphy.)

if there is a tenant in it, you could oust him if you wanted to move in yourself.

The Witness: My recollection, your Honor, is they had a hard time ousting them.

The Court: From a practical standpoint, that could have been true, but my understanding is under rent control, while you couldn't normally oust the tenant, if a person bought property to live in as his own home, they could do it. But, all right. If counsel has anything he wants to explain about it further, he will ask you.

Q. (By Mr. Chehock): Now, did you testify a while ago you thought single-family houses were better from a selling standpoint than duplexes?

A. Yes, sir. [196]

Q. That was not the opinion of Artcraft, was it, and you folks back in those years at the time you wanted to sell these?

A. My opinion has always been and still is a single-family house is easier to sell than a duplex.

Q. I call your attention, Mr. Murphy, to the wording of the ad of May 4 in the Los Angeles Herald Express that states, "One apartment vacant in each building, ready for purchaser to move in immediately at close of sale. Rent of the other apartment will carry payments on the building."

What does that mean?

A. I didn't write this ad. "One apartment vacant in each building," that means we had evidently ten vacancies up there.

Q. One of the units of the duplex was vacant?

(Testimony of William K. Murphy.)

A. That is correct.

Q. It means the other unit in the same duplex, the rent from that would carry the payments on buying it, isn't that true?

A. That is what this says.

Q. So it was advertised as a sales advantage, wasn't it?

A. As I said before, I did not write the ad and never approved it before it was put in. I don't know just what Mr. Boland had in mind when he wrote it. [197]

Q. Now, I refer you to the ad in the Los Angeles Herald Express of May 11, 1946. Will you state there who it is that is being advertised as selling these two places?

A. "For sale duplexes, Artcraft Builders, Inc.," is at the bottom of the ad.

Q. And who does it say it is being sold by?

A. Being sold by the builders.

Q. Would you say that is the representation to the public that the Artcraft is selling the houses?

A. According to the ad, I would say that the builders were selling the apartment building.

Q. Who were the builders?

A. Artcraft Builders, Inc.

Q. You notice also that in this same ad it carries the same thing, "Rent of one apartment will carry payments on building," is that right?

A. Yes, sir.

Q. I refer you to an ad that appeared in the Los Angeles Herald Express, May 18, 1946. These

(Testimony of William K. Murphy.)

ads in May, 1946 refer to the 70 duplexes here in controversy, is that right? A. That is correct.

Q. Will you state to the Court, does that not represent that the duplexes are being sold by the builder and the ad is under the name of Artcraft Builders, Inc.?

A. It says, "For sale duplexes by builder," and [198] "Artcraft Builders, Inc." is on the ad.

Q. Will you state also up at the top what it says there? A. You mean the third line?

Q. Yes, the third, fourth and fifth.

A. "Had 70 two weeks ago. 20 left. The reason, they have two five-room apartments each. Are almost new."

Q. Isn't that another instance of the Artcraft Builders representing to the public that the duplexes are a good sales advantage because of the fact that they are duplexes and the reason they have made fast sales is because they are duplexes?

Mr. Axelrad: Your Honor, I object to this constant repetition about asking the witness to draw a conclusion based on something not in evidence that Artcraft is representing to the public.

The Court: This is cross examination.

The Witness: I forget what you asked me.

Q. (By Mr. Chehock): That ad is a representation to the public that the reason the duplexes are being sold is because they are duplexes and because the one buying them has the benefit of the rental from one unit to make the payments on the purchase for the duplexes, isn't that right?

(Testimony of William K. Murphy.)

A. Yes. Rent of one will carry the building, it says [199] in this ad, also.

The Court: I may say, just by way of comment, I think that those ads——

Mr. Chehock: Speak for themselves?

The Court: Yes, they speak for themselves.

Mr. Chehock: I think you are right, your Honor.

The Court: I don't think any reasonable man would look at that and conclude that the ad was not intended to carry that implication.

Q. (By Mr. Chehock): Are you acquainted with this ad of May 19, 1946, in the Los Angeles Examiner?

A. I haven't been acquainted with any of them.

Q. You do know that they were advertised in the Herald Express and the Los Angeles Examiner, is that not true, the 70? A. Yes, sir. Here is one.

Q. The same ad in substance that you have just read was in the Los Angeles Examiner, is that not true? A. Yes, sir.

Mr. Chehock: I think the thing speaks for itself, your Honor.

The Court: All right.

Mr. Axelrad: Your Honor, may I ask a question at this point? [200]

The Court: You may.

Mr. Axelrad: The question I would like to ask is, what is Mr. Chehock trying to prove by this line of questioning. The issue in the case, as I understand it, is whether Mr. Murphy and Mr. Pool and

(Testimony of William K. Murphy.)

their wives are in the business of selling houses, and not whether Artcraft was in the business.

The Court: I don't know exactly what Mr. Chehock is trying to prove by this, if anything.

Mr. Axelrad: It seems to me to be irrelevant.

The Court: It is cross examination of this witness. We can ask him if he has some statement of what he is directing it to.

Mr. Axelrad: This doesn't contradict anything my witness has said, at least this line about the advertising. I was wondering what the relevancy is to any of the issues in the case.

The Court: I don't know whether it contradicts anything your witness has said, and I won't until I review the evidence.

Mr. Chehock: I think the record will show that Murphy and Pool have used the corporation whenever they see fit for their advantage, and that this is another instance. Artcraft had the reputation of being a builder of houses for sale and they are selling houses here, although actually [201] title had been transferred to Murphy and Pool. It is all in the family. It is further evidence of the fact that these houses were held primarily for sale.

Mr. Axelrad: Your Honor, everything but that last statement I think is a very serious admission that he is trying to attribute the corporate activities to Murphy and Pool, when the corporation did do many things for them and paid a tax, and their very separateness is one of the issues in this case.

The Court: If that is an admission, at the

(Testimony of William K. Murphy.)

proper time you can argue it, but let's get along with the evidence now. Most of this is argumentative rather than proceeding to get the evidence in. A lot of the questions have been argumentative to some extent.

Q. (By Mr. Chehock): Are you acquainted with the advertisements that were put in the Los Angeles Times and the Herald Express and the Herald Examiner of the 100 duplexes?

A. No. I can't say I am familiar with them.

Q. By looking at that particular advertisement, would you say that some of those ads represented on the 100, also, that the builder was selling them?

A. That is what the ad says. This ad doesn't say it, but this one does so.

The Court: Well, it says what it says. Does that [202] have to do with the 100?

The Witness: That is 13,000. That is what the 100 were sold at, your Honor.

The Court: That ad does have to do with that?

The Witness: That is correct.

The Court: Whoever put it in, it does have to do with that.

The Witness: Yes.

Q. (By Mr. Chehock): Who put these ads in the paper for the 70 and the 100?

A. Mr. Boland.

Q. Did he show the ads to you for your approval before they were put in?

A. I don't remember him showing me any.

Q. Did he show them to either you or Mr. Pool?

(Testimony of William K. Murphy.)

A. I don't remember him showing any to Mr. Pool.

I might add, if I may, your Honor, I went fishing the first of May and I think I was gone about two weeks, so that is when it started. There were two of those ads in there during the time I was fishing.

Q. Were written leases made on the 22 structures in 1946, 1947 and 1948 the 22 apartments you refer to here as the 22?

A. Yes. In 1946, 1947 and 1948? [203]

Q. Yes.

A. I don't remember whether they were made in 1946, 1947 and 1948 or not. We had written leases on them in 1946, I know.

Q. You testified, I think, that in March or April, whenever you talked to this attorney, that you stopped taking written leases on the 70 and 100. Did that apply also to the 22?

A. No, sir. The 22 were one-bedroom.

Q. And you continued to take written leases on those?

A. Well, we took them for quite a while. I have all the leases. I will be glad to bring them in to you.

Q. For how long a period did you take written leases on these 22, approximately?

A. I would say up until—I don't know. I know we had them in 1946, and probably had them in 1947. We had leases on them when the rent control raised the rent on them. I think that was in 1948. So we did have leases on them in 1946, 1947 and 1948.

(Testimony of William K. Murphy.)

Q. Did you hire Mr. Boland to sell the 70 and the 100 at the same time? A. No, sir.

Q. Do you think there is an exchange of letters or something in writing there, but you can't find it?

A. My recollection was that he had written me a letter— [204] he came down there and talked to me and Mr. Pool at least ten different times trying to get us to sell him the stuff. My recollection was, as I stated in my testimony, that he wrote us a letter or we wrote him a letter, but, as I said, that file was taken—I haven't been able to find that letter. I have been able to dig up everything else that they have wanted, but I have looked and looked and looked. The fact of the matter is I couldn't say positively there was a letter.

Q. The 70 duplexes, I think you testified, went very fast, within five or six weeks, is that right?

A. Yes, sir.

Q. In other words, there was a great demand, is that right? A. Yes, sir.

Q. Why did you employ Boland to sell the 100 since they went like hot cakes? Why did you agree to pay him $50,000.00 for selling these 100, if there wasn't any particular effort required?

A. Well, we weren't in the real estate business and we didn't want to be bothered with them. There was a lot of effort required. In order to make a sale, you have to first show the property. Then you would have to sell it to the people. Then you would have to arrange the financing. Then you would have to open an escrow. Then you would have to [205]

(Testimony of William K. Murphy.)

check their credit. I don't know what else is required, but I know that much is required and we didn't do any of that.

The Court: Is what you are saying that you didn't want to be bothered with the incidents and the tasks that would enter into the act of selling to the customers, is that it?

The Witness: What I am trying to convey, your Honor, is that we weren't in the real estate business and we didn't want to get into it.

The Court: Of course, you were in the real estate business of a certain kind; even if you were in a rental business, you would be in the real estate business. That is a part of real estate business. That is a pretty broad term. You weren't real estate brokers and you weren't doing that sort of work.

The Witness: That's right.

The Court: All right.

Q. (By Mr. Chehock): Tell me, Mr. Murphy, just what did you and Mr. Pool do in 1946?

A. Well, we didn't do anything.

Q. If you were paying Mr. Boland $85,000.00 for his work when you and Mr. Pool weren't doing anything, it looks rather peculiar, doesn't it? [206]

A. It doesn't to me. That was the contract I made and I usually live up to my contracts. I did not intend to pay Boland, and I don't think Mr. Pool did, $85,000.00 for selling those buildings and then turn around and do the work for him.

Q. I know, but since you and Mr. Pool weren't

(Testimony of William K. Murphy.)

active in doing other things, of course, there was some work involved with it, but when you weren't doing anything, why did you agree to pay him $85,000.00?

A. We hired Boland the same as a cement contractor or a plasterer, or someone to do the painting or any other contractor. I didn't think there was anything peculiar about it.

Q. The houses weren't there for rental, so you didn't have to rent them since you were selling them, and the houses were being sold and you didn't have anything else to do, and still you say you agreed to pay Boland $85,000.00. There must have been some reason.

The Court: What difference does it make, Mr. Chehock? A fellow might own an apartment house and operate it, yet he wouldn't want to do it himself, even though he was loafing. He might hire a manager to do it. He would be putting out the money.

Mr. Chehock: It is possible, your Honor. $85,000.00 is quite a bit, and especially if you aren't busy. [207]

Let me ask this question and I think you can understand why I am inquiring:

Q. (By Mr. Chehock): Isn't it true, Mr. Murphy, in making the decision on whether or not you would sell the 70 and the 100 duplexes, you were advised taxwise that it would be better to have someone else sell them rather than you?

A. That is absolutely not true, positively, no.

(Testimony of William K. Murphy.)

The Court: It wouldn't make any difference, anyhow, even in this case, because he has testified here that houses they built for sale they sold through a broker rather than selling them themselves, which is indicative of the matter that we had such a discussion on here Friday. The fact that he sold through a broker or directly doesn't particularly mean anything in these cases. It is just one factor. But here we have the testimony with respect to the sale of houses they were selling through a broker over in New Mexico and Denver.

Mr. Axelrad: Your Honor, that was a corporate activity of the builder that was building them for sale.

The Court: That is exactly the point. They were building them for sale. The fact that they sold through a broker didn't make them any less building for sale and wholly for sale.

Mr. Axelrad: It wouldn't even occur to us to call [208] that capital gain.

The Court: Certainly. The fact that they sold through a broker wouldn't make any difference. I think I had that question up, if I am not mistaken, in Jacob Gruver in the Washington area in around 1940, 1941 and 1942. Jacob Gruver very strenuously contended I was required to hold he was not in business because he didn't do any of the selling himself, he sold through brokers.

Well, very obviously, when all the facts were in, Jacob Gruver was in business and he was holding his property primarily for sale to customers. It

(Testimony of William K. Murphy.)

didn't make any difference whether he sold them himself and went through the work of negotiating the sale or whether the broker did.

The Witness: I don't know whether I made it plain, your Honor. May I say something?

The Court: Your counsel can ask you or government counsel can ask.

The Witness: Yes, sir.

The Court: I think we wander off on a lot of inconsequentials more often than not on these volunteered statements.

Q. (By Mr. Chehock): Mr. Murphy, just so the record shows, when were you born? A. 1899.

Q. When was Mr. Pool born?

A. He was born in 1889. He was ten years older than I was.

Q. In regard to the 70 duplexes and the 100 duplexes, since the loans, FHA loans, were in excess of the cost and since there was no personal liability assumed, you didn't even have your credit invested, did you? A. Have our what?

Q. Your credit. What did you have invested actually in building the 70 and 100 houses or units? You had none of your own funds invested in building the 70 and in building the 100, is that right?

A. We had no funds invested, that is true.

Q. Isn't it true also that in view of the FHA loan payments and the rent ceilings, that you had no opportunity to make substantial profits from the 70 duplexes and the 100 duplexes except upon sale of the properties?

(Testimony of William K. Murphy.)

A. We could have sold the properties the day after we built them for twelve thousand. I don't know whether we had a buyer, but we were allowed to. The law allowed us to sell for six thousand a unit the day it was finished.

The Court: But you couldn't sell them for over six thousand?

The Witness: That is correct, yes, sir.

The Court: Right in that connection, just in case [210] it is of some moment, when you get down to your argument and you are preparing proposed findings and making your argument, I notice in the stipulation, Paragraph No. 15, beginning at the bottom of page 7, reference is made to Exhibit H-8-A to -D, on National Housing Administration orders, the numbers are given and that they are applicable to the projects here involved in Tracts 11451, 11674, and 13163.

Am I right in assuming that the stipulation also shows that those are the tracts on which these three groups of buildings were built?

Mr. Axelrad: That is correct, your Honor.

The Court: All right. Now, these regulations contain certain restrictions, and among them is the restriction mentioned, that in case of the sale to tenant, and in certain circumstances to someone else, total purchase price shall be the fair market price or $6,000.00, whichever is lower.

Then in other places here it states that these things are binding during the emergency. Well, one paragraph under Sales to Tenants in the second

(Testimony of William K. Murphy.)

one of these, H-8-B, says the occupancy and disposition provision shall continue to apply to such housing after the option is exercised or terminated for the duration of the National Emergency declared by the President on September 8, 1939.

I find other references in some of these where it [211] mentions these things are binding for the duration of the National Emergency declared by the President on September 8, 1939.

Now, whether or not my recollection is correct on these matters having to do with these matters of national housing, I don't know, and wouldn't know without checking up. As a matter of fact, I don't know whether I ever knew or not. I have heard and read some things on some of them. But that statute which provided for declaration of national emergency, it is my understanding it also carried a provision which would permit a similar declaration that the emergency had ended and that these sections were terminated.

I know that there were some executive orders that follow the end of hostilities in August, 1945, and we have had various executive orders starting and ending things ever since. As a matter of fact, we had some just a week or two ago on OPS.

I trust if anything is going to turn on those things, and it seem to me quite likely it would develop that there would be some bearing that might come into play in view of some of the questions that have been asked as to whether or not any of these emergency restrictions in these orders, which the

(Testimony of William K. Murphy.)

stipulation says are applicable to these tracts, whether any of the emergencies that are covered in those orders were declared at an end any time in a period [212] which would have a bearing and effect on this question and problem that we have before us, if that is true, I just mention that because I want to make sure that the record is complete, and if it is not already, if there is any such thing and it is not already covered by the stipulation, I just want to say that I am depending on you gentlemen to see that those things do come into the record, if there are any, before this case is closed.

Mr. Axelrad: I would like to suggest, your Honor, on the stipulation, if Mr. Chehock is willing, on the date on which these NHA restrictions were revoked by Executive Order, which is October, 1945, the date he was examining the witness about, at that time I want to make a clarifying statement there never was any control on other housing.

What I was objecting to at the time was the suggestion——

The Court: What do you mean by "other housing?"

Mr. Axelrad: On nonpriority housing. In other words, there was no price control on houses. There were priority restrictions.

The Court: There was plenty of restriction on any building during this National Housing program.

Mr. Axelrad: Yes, and those are the ones that went off in October. Mr. Chehock has used that for two purposes: To show when these restrictions

(Testimony of William K. Murphy.)

went off, and then [213] he tied it into a sudden rising market price. We will have witnesses that will show what they think entered into that.

The Court: I don't know how these buildings were built and how the money that was borrowed—I judge some, if not all of it, came out of the banks and was insured—was handled, and I don't know whether it would have any bearing of any particular importance on the questions we have to decide, but I do know that some of these housing developments, the NHA, the FHA, or some of those agencies in these periods, rode very, very strict herd on specifications. They rode herd on seeing to it that the progress was maintained in the construction and that the work done measured up to requirements. Otherwise, the money in these loans, even though borrowed from Prudential Insurance and the like, was not forthcoming.

I don't know whether there is anything like that in this case, but I do know that is true on a lot of them. I mention that at this time because much has been made of this restriction as to the price at which these units could be sold, and I have had those things on my mind because I don't want the record closed with something that ought to be here absent.

Mr. Axelrad: The stipulation shows all three tracts we have been discussing were built under priorities approved by the War Production Board, and the applications with their [214] approval are in the record as exhibits to the stipulation. All that

(Testimony of William K. Murphy.)

is lacking is when these restrictions were revoked.

The Court: At a proper time, then, let us complete the record.

Mr. Chehock: Your Honor, I would like to make a statement in that regard. I have tried other war housing cases, and I thought it was a matter of open knowledge, perhaps something the Court could take judicial notice of, that is, the ceiling was lifted October, 1945 on the selling price. I can quote the exact language of the San Jacinto Homes case, which was decided——

The Court: Well, before you go into it, all I am saying to you is that if there is any question about it, let's complete the record. I don't care how it is completed. If it is clear, I can reach it that way, I might do it that way, but it would be a whole lot easier if it was right in this record and I didn't have to go scrambling around looking for something, even if I could take judicial notice of it.

Mr. Chehock: I agree with you, and I think counsel should do it, but is petitioners' counsel willing to have the Court take judicial notice of any of these matters we are just talking about in the event we can't find it?

Mr. Axelrad: Mr. Chehock, we can find it. As you say, it is October, 1945 and we are both in agreement. Let's stipulate and be done with it. [215]

The Court: Between now and tomorrow morning you gentlemen have a little get-together and agree on what is to go into the record on it. Then if you have any difficulties, I will see if I can help out.

(Testimony of William K. Murphy.)

All right. Go ahead.

Q. (By Mr. Chehock): In 1946 and 1947, when these 70 and 100 duplexes were being sold, I believe you testified on direct examination that Mr. Boland used the offices of Artcraft and Edward Pool and Associates. Is that right?

A. It was Artcraft Builders' office.

Q. But it was the office used by both Artcraft and Edward Pool and Associates, is that right?

A. No. It was Artcraft Builders, Inc. office and they kept Edward Pool and Associates books there.

The Court: Did Edward Pool and Associates have any other office?

The Witness: No.

The Court: All right. Go ahead.

Q. (By Mr. Chehock): Were you the office man and Mr. Pool the outside man in your enterprises?

A. Well——

Q. Who was in the offices most of the time, you or Mr. Pool? [216]

A. Well, I was in the office and out of it. We had a general auditor, Mr. George C. Clark, who really was in the office all the time. I had charge of the office, however. I was custodian of the records and the books, but I was out of the property quite a bit.

Mr. Pool done all the construction end of it. He was out all the time. I would say I was in a lot more—90 per cent more than Mr. Pool was. My work was in charge of the office.

Q. In 1946 and 1947, what did you do in this

(Testimony of William K. Murphy.)

office building, either for Artcraft or for Edward Pool and Associates?

A. I didn't do anything.

Q. Did you go to the office?

A. I used to go when I was in town, yes, sir.

Q. Did you have to confer with Mr. Boland occasionally?

A. Oh, I talked to Boland when I would go down to the office, yes. I don't know what I conferred with him about, but I talked to him, yes, sir.

Q. You and your associates there had to sign deeds on all these properties, didn't you?

A. We had to sign the deeds for the 70 properties, and we left them in the safe there. We went marlin fishing, as I remember it.

Q. What about the 100? [217]

A. I don't know. I think when we started selling the 100, they had deeds made up and I think we signed those in September or October sometime. I don't know whether we signed all the 100 or not. We signed the 70.

Q. Wasn't usually your signature left off until the time of the sale?

A. No, not that I remember. I don't know. I don't remember.

Q. You had to sign the escrow papers.

A. Sign the what?

Q. Escrow.

A. I think we signed the escrow papers, yes.

Q. There were 170 of those to be signed, weren't there?

A. On both tracts, yes, sir.

(Testimony of William K. Murphy.)

Q. Yes. A. There were 340.

Q. Where did you do all this signing and all this work?

A. Well, when an escrow was opened and we were notified it was opened, I don't know whether I went down to the bank and signed them or they mailed them out to us. I think they mailed them out to us, but I am not positive, though.

Q. Your business headquarters in 1945, 1946 and 1947, was in this one building down there on the tract, that is the only office building you had, wasn't it? [218] A. Yes, sir.

Q. How much of the time in 1945, 1946 and 1947 did you devote to your business?

A. Well, I retired in July or August 1945—no. In 1946, yes. Well, I went down there and signed the deeds and whatever I had to sign to collect for the property, but I wasn't down there every day by any stretch of the imagination.

Q. Well now, Arteraft Builders, Inc. handled the rentals of these properties for Edward Pool and Associates during the time you were renting, isn't that right? A. Yes, sir.

Q. You were the active head of Arteraft Builders, Inc., weren't you? Who contacted the rentals, such as there were?

A. Who collected the rents, you mean?

Q. Who did the work?

A. Mrs. Woodruff, Mrs. Hoover, and our general auditor and another lady.

Q. All under your supervision?

(Testimony of William K. Murphy.)

A. I was secretary and treasurer, Mr. Clark was the general auditor, and the other three were bookkeepers.

The Court: Were they paid salaries?

The Witness: Yes, sir.

The Court: By whom?

The Witness: Arteraft Builders, Inc.

Mr. Chehock: I am going to make some inquiries, [219] your Honor, with respect to Exhibit N-14 and O-14, and it might be helpful to the Court if you had them before you.

Q. (By Mr. Chehock): Mr. Murphy, do you know any reason why the deeds on the 100 duplexes were not put up at the time the escrow agreement was entered into or almost about the same time?

A. You never put a deed up until you qualify the purchaser. In other words, if you bought a house from me or from a real estate broker, Mr. Boland in this instance, the first thing he would have to do for FHA would be to check the man's credit, check his bank account, verify his employment.

Q. If he didn't meet the requirements or didn't get the money, the escrow wouldn't be effective, would it? I mean it wouldn't go through?

Can you think of any reason why the deed wouldn't be executed and put in escrow awaiting the determination of whether or not the purchaser would meet the escrow requirements?

A. Why, that isn't customary even today. We don't do that.

(Testimony of William K. Murphy.)

The Court: I don't know whether I follow either one of you on that. Give an illustration.

Mr. Chehock: All right. [220]

Q. (By Mr. Chehock): Referring you to Exhibit N-14, which is Tract 11451 on the 70 duplexes——

The Court: All right.

Q. (By Mr. Chehock): ——and escrow dates, which is in the middle of the sheet there, under that there appears the date of the escrow instructions, and then the second column over from that is "Grant Deed dated." You will notice on this Exhibit N-14 for the 70 duplexes, it was put in escrow on May 24th and the deed was executed on May 28th, which is four days later.

On the second lot there, it was put in escrow on July 29th and the deed was executed on the date August 2nd.

On the third one, it was put in escrow on June 10th and the deed was dated June 11th.

On the fourth lot, Lot 4, the property was put in escrow on June 29, 1946, and the deed was dated three days later, on July 2, 1946.

On Lot 5, on July 30th it was put in escrow, and the deed was executed on August 1st, the very next day.

The Court: Now drop down to No. 7.

Mr. Chehock: 7 seems to be an exception. It was put in escrow 6-10 and the deed was 7-9.

Lot 9 and Lot 10 and Lot 11 were all made within [221] two or three days, 1, 2 or 3 days of the time.

(Testimony of William K. Murphy.)

The Court: There is a longer one on 12 and 13.

Mr. Chehock: That's right.

The Court: All right. Now you have got those illustrations in. What is the purpose?

Mr. Chehock: I refer you to Exhibit O-15 for Tract 13163. First I will refer you to those that are not made in August, prior to September 21, 1946, which would be six months from the date of the deed of March 21st.

I refer you to the third lot, which was made January 23, and the grant deed was made four days later.

On the one made on Lot 5, it was put in escrow November 2nd and the grant deed was made November 4th.

Lot 6 was put in escrow November 14th and the deed was dated November 15th.

The Court: Well now, what about it? What is it you want to know about that?

Mr. Chehock: In view of this, I would like to ask the witness then how it comes that those that are put in escrow in August, without exception, the deeds are not made until sometime subsequent to September 21, 1946. Lot 1, for example, was put in escrow August 14th and the deed was made September 23rd, which is two days after the six months.

Lot 2 was put in escrow on August 20, 1946——

The Court: Well, wait a minute. Lot 1, according [222] to my sheet, has August 14, 1946, for the date of the escrow instructions.

Mr. Chehock: Right.

(Testimony of William K. Murphy.)

The Court: And the deed of grant is September 23, 1946.

Mr. Chehock: Right. That is my point.

The Court: The next one, however, does extend more than six months. It is August 20, 1946, and 3-10-47.

Mr. Chehock: Yes.

The Court: The first one is only about a month and nine days.

Mr. Chehock: Lot 2 and Lot——

The Court: The same is true of Lot 4.

Mr. Chehock: Of Lot 4 and of Lot 8.

The Court: Yes.

Mr. Chehock: In those four situations, you will find that those put in escrow in August, the deeds were not put up until sometime subsequent to September 21, which is a lapse of a month or over, or about that, and some of them even more than that, whereas the others were put in escrow within a matter of a few days, generally speaking.

Mr. Axelrad: Your Honor, I object to this line of questioning on the ground that the hypothetical examples he puts are not representative to start with.

The Court: He can't get it all done at one time. [223] If this witness knows the answer to the questions, let him answer.

The Witness: I would like to know if those are the escrow dates. We signed the deeds whenever they were given to us to sign. Or are those things some exceptions?

(Testimony of William K. Murphy.)

Mr. Chehock: This schedule is made up by Mr. Lampe, your own man, and we stipulated these are the dates. If you say this is not a representative example, let's carry through the whole thing.

Mr. Axelrad: Your Honor, he is suggesting very plainly, without saying so, that they delayed putting the deed in escrow until the six months' period, which is completely irrelevant, if true. Let's take the second one which is in August 1946. Then they only had to delay until the next month, but they actually delayed to March 10th. Why do they need a whole year?

Mr. Chehock: That is true, but that date is subsequent to September 21, and that is my point.

The Court: What is this about six weeks?

Mr. Chehock: It is six months.

Mr. Axelrad: We are talking about a holding period. His point is there may not be a six months' period in all these things.

The Court: What difference is there between a six weeks' holding period and a two days' holding period? [224]

Mr. Axelrad: Six months.

The Court: I am saying six weeks.

Mr. Axelrad: There is no six weeks' problem, your Honor, that I know of.

The Court: I am asking if there is any.

Mr. Axelrad: No.

The Court: No. 1 was about six weeks.

Mr. Axelrad: The holding period relates to the

(Testimony of William K. Murphy.)

March date in 1946 when the Associates acquired title to all these.

The Court: Oh, is that what you are talking about?

Mr. Axelrad: Yes.

The Court: All right.

Mr. Chehock: The deed to the 100 duplexes under date of March 21, 1946.

The Court: I wasn't advised of that, except way back there somewhere.

Mr. Chehock: Six months from March 21 would be September 21.

The Court: All right. Go ahead with your question.

Q. (By Mr. Chehock): Just go through the schedule here. In O-15, the only ones put in escrow on the first page are the ones we have already mentioned.

On page 2 you will find Lot 17 was put in escrow [225] on August 21 and the deed is dated a month and five days later, on September 26.

Lot 18 is put in escrow August 19, and the deed is dated December 2nd.

Then on page 3, Lot 21, which was put in escrow September 21 and the grant deed was made September 26, only five days, but you will notice that is subsequent to September 21.

Then on Lot 28, it is put in escrow August 21 and the grant deed was dated September 26.

On page 4, on Lot 36, it was put in escrow August

(Testimony of William K. Murphy.)

21, 1946, and the deed was dated September 26, 1946, a month and five days.

Lot 28 was put in escrow August 21, 1946, and the deed was dated September 26, 1946.

The Court: I think you can shorten this, can't you?

Mr. Chehock: It is true of every one of them.

The Court: You can shorten it by noting that none of them came out, insofar as the deed is concerned, prior to September 21, 1946. That is true of all of those.

Mr. Chehock: I would like to ask the witness if he can answer as to why most of the other escrows on all other lots, on the 70 and on all of the 100, why it took such a long lapse to put those deeds in that were put in in August, and not after that. [226]

Mr. Axelrad: He is assuming a fact, not only not in evidence, but contrary to the very exhibit. He is saying there is about a month's delay in some of the early ones and there isn't that much in any of the others.

Mr. Chehock: I didn't say any of the others, but the great majority.

Mr. Axelrad: I can point to a delay as much as a month or six weeks being very common in escrows after that date.

The Court: Not very common. There might be a few of them, but it isn't very common.

Mr. Axelrad: This is the first time I was advised of this particular development, so I hadn't been prepared, but I notice a great number of them.

(Testimony of William K. Murphy.)

The Court: I have been through them, too, and most of them are not. There are a few that are of a little longer period, but most of them are one to four days, three days, usually, one, two, three, more often than not. There are a few of them that will run two weeks, or some of them will run a month.

Take No. 16 on Exhibit O-15.

Mr. Axelrad: No. 6?

The Court: No. 16 on Exhibit O-15.

Mr. Axelrad: That is November 14th to November 15th. [227]

The Court: No. November 18th to December 10th.

Then you can drop down to 19 on the same page, December 4th, for the first date as against December 30th for the last.

Mr. Axelrad: Those are some I had in mind.

The Court: But those are in a decided minority as far as that is concerned. I don't know whether it makes any difference, but let's get on here and finish your objection.

Mr. Axelrad: The ones he has referred to, as far as the number that are sold are in the decided minority, and I would suggest that while these are in the minority, they number about the same delay as in the early ones.

The Court: The ones he is talking about, the others, are the August dates.

Mr. Axelrad: Yes

The Court: The bulk of the August dates are about three to five weeks or more, three, five, six.

(Testimony of William K. Murphy.)

Some of them run more than that. So you are wrong on your analysis there. But what is the objection?

Mr. Axelrad: The objection was that he said that they ran longer, and I assume there he meant on all these cases where you find many a delay of three or four weeks in the other group that were later, like you pointed out.

The Court: I didn't say many. I said a few.

Mr. Axelrad: All right, a few, but I think there [228] are a good dozen.

The Court: Yes.

Mr. Axelrad: Out of 100 houses.

The Court: That is still a few.

Mr. Axelrad: It is a matter of degree. I thought it was many, your Honor.

The Court: It is relatively few as related to the others.

Mr. Axelrad: All right.

The Court: Now, I think what you better do, I am going to allow this questioning to go on, the inquiry to be made, but in the light of the discussion and how far we are from the question, I think we will turn back and have the reporter find the question and read it, and then I think you can do a better job of making your question, because I do think it could be made clearer. Attend carefully when he reads it and then take a little time in phrasing your question.

Now, we will have to give the reporter an opportunity to turn to the question, because if we interrupt, he will have to start writing again.

(Testimony of William K. Murphy.)

Mr. Chehock: I would be very happy to rephrase it without waiting, but either way is all right.

The Court: In the light of the discussion we have had, it might be just as well to have the question reread. [229]

(The question was read.)

Mr. Chehock: I think you are right. I think I should reframe it.

The Court: Take your time before you start asking.

Q. (By Mr. Chehock): Mr. Murphy, as Exhibit O-15 shows, all of the sales in which the escrows were placed, the property was placed in escrow prior to September 21, 1946, since there was a lapse there of all of those placed in escrow prior to September 21 of a time sufficient to have the deed placed in escrow subsequent to September 21, while in all other sales, both of the 70 and of the 100 duplexes, with some minor exceptions, the deeds were dated within a few days of the escrow, can you explain why this happened?

I don't think that is too well worded, either.

The Court: If the witness can answer it, he may. It is better than your other one.

The Witness: I could probably have answered it a long time ago, your Honor. I was not in the city between August 15 and about the 10th of September. I can take up that much of the time, and neither was my wife.

The Court: Well, there was a lapse of about five weeks between August 15, 1946 and September 21,

(Testimony of William K. Murphy.)

so apparently you were in the city then. Suppose you continue your answer, if you have one. [230]

The Witness: Well, I presume that when I got back, that these deeds were drawn up, printed, and when they were submitted to me, why, I signed them. I don't know when Mr. Pool signed them. He may have signed his copy in August.

Q. (By Mr. Chehock): When were you out of the city?

A. Between August 15th and between the 8th and 10th of September.

The Court: I thought you said you were back by the 15th of August.

The Witness: No, I didn't leave until the 14th of August.

The Court: All right.

The Witness: I went up to the Lodge in the High Sierra and we went from there to Sioux City, and then back, with my wife and family.

Q. (By Mr. Chehock): Can you explain to the Court what these two boxes are here? Tell us what they contain? A. No.

Q. Do you know what these files are right here?

A. Let's see one of them.

The Court: Show him some or maybe you can go down and look at them.

The Witness: I can go down there, if that's all [231] right.

The Court: Do that, please. Just hold them there and let him look at them.

(Testimony of William K. Murphy.)

The Witness: I think I know what they are, but I will look.

(Witness leaves stand and goes to counsel table.)

The Witness: These are files in the 70 and 100 duplexes. Those are the Boland realty files, however, not Arteraft Builders.

Q. (By Mr. Chehock): Am I correct that either you or your counsel made inquiry of the bank of America, who handled these properties in escrow, and you were advised that they had destroyed their escrow papers? Is that true?

A. What was that?

Q. Is it true that either you or your counsel contacted the Bank of America, who had these papers in escrow, and they informed you that their escrow papers on these transactions had been destroyed?

A. No. I never contacted the Bank of America. To my knowledge, there is supposed to be a copy of each escrow paper in the files, and I think there was, to my recollection, when I turned them in for your inspection.

Mr. Chehock: May I ask Petitioner's counsel whether he made inquiry and if he found out whether or not [232] the files are available?

The Court: Do you ask him?

Mr. Chehock: I am asking Petitioner's counsel.

Mr. Axelrad: Mr. Chehock called for the escrow papers, and as I say, we were laying out everything he wanted in our offices, so I called the Bank of

(Testimony of William K. Murphy.)

America in Long Beach and talked to somebody, who purported to be the vice president, who put me in touch with the clerk in the escrow department, and she informed me they did not retain them that far back, and she thought they had been destroyed.

The Court: All right.

Q. (By Mr. Chehock): In regard to the 70 duplexes that were sold, I have here a couple of them and ask you if you know whether or not this is a typical type of deposit slip that was signed by Mr. Boland and the purchasers at the time the 70 duplexes were acquired.

A. You mean at the time they were sold to the purchasers?

Q. At the time the deposit was made for purchase of the 70 duplexes.

A. I think it was, yes.

Q. I notice that there is appended to this, the particular one I have, covering Lot 32, Tract 11451, in which the deposit contract is signed by Phil Boland and Mr. [233] and Mrs. Campbell, bears date May 5, 1946, and among the same papers I find a grant deed which is a printed deed bearing the notation of the fact that it covers land in Tract 11451. The deed is dated June 4, 1946. I notice, also, that the deed is made out bearing the names of you people down there where the notarial acknowledgment is taken. Do you know anything about the printing of these deeds? A. No, sir.

Q. I find here, also, a copy of what purports to be the escrow instructions. Would you look that

(Testimony of William K. Murphy.)

over and state as to whether or not that would be a typical type of escrow instruction that was entered into on these 70 duplexes? If you want to, you can look through all of these.

A. Well, these escrow instructions are not signed.

Q. Those are the copies.

A. Yes. Well, I would say yes. I don't know, but I take it they were.

The Court: This is something that should have been agreed to, I would say. We oughtn't to have to take up time with this sort of thing, if that is all they were.

Mr. Axelrad: Mr. Chehock wanted me to agree that the contents of a given folder was typical of all the papers in all the others, and we went through them, and I found they varied in appreciable details, and were not the same. I couldn't see the relevancy of any of them and I [234] didn't feel I should stipulate to something that was not so.

The Court: The rules take care of the method of handling those things. If they are true, that is one thing. If you want to make objection to something being immaterial and irrelevant, that is done when the stipulation is offered, but that doesn't deter the applicability of our rules about stipulating such matters.

Mr. Axelrad: It was impossible to stipulate these are all alike, because they aren't. That is the difficulty, to start with. Since I didn't know which ones

(Testimony of William K. Murphy.)

he considered relevant, I couldn't stipulate to any part of it.

The Court: At least you could stipulate certain papers cover certain particular sales.

Q. (By Mr. Chehock): Let me hand to the witness all of them on the 70 and let him look at the form of the deposit contract that was originally entered into between the purchasers and Mr. Boland and have him state whether or not the one I have just referred to him is typical of all of them.

A. Are you talking about a sales slip? You said escrow instructions.

Q. First, I am saying about the original contract entered into between Phil Boland and the purchasers.

A. In sum and substance, I think it is the same. I think they are all the same. It may be worded a little [235] differently.

The Court: Well, it is 5:00 o'clock. I think those things can be examined outside of the formal hearing and those items that can be agreed to where there is no dispute about the agreement, can be reached to that extent. If there are some where there are differences, those differences can be presented. So I will leave it to you gentlemen.

We will recess now until 10:00 o'clock tomorrow morning.

(Whereupon, at 5:00 o'clock p.m., an adjournment was taken until 10:00 o'clock a.m., Tuesday, March 3, 1953.) [236]

The Court: We will resume trial in the Pool, Murphy and Arteraft incorporated cases.

Mr. Chehock: I think since last night, your Honor, we have made some progress in agreeing on what can go into the record and as to some of these instruments.

The Court: All right.

Mr. Chehock: Do you want to go ahead first?

Mr. Axelrad: We have an oral stipulation on a few things that will save some time.

The Court: That is fine.

Mr. Axelrad: The 100 duplexes were all rented on a one-year lease from the date of completion, and those leases expired depending on when the building had been completed, in either June, July or August of 1946.

The Court: All right. Is that agreed to?

Mr. Axelrad: And September. There were some in September.

The Court: All right. The record will show that.

Mr. Chehock: We so stipulated, your Honor.

The Court: All right.

Mr. Chehock: Of course, there were a number of these leases that were entered into at that time that were canceled.

That is true, isn't it, counsel? [239]

Mr. Axelrad: That's right. When people were transferred out, it was the custom of Arteraft or the Associates to release them from the lease and then the buildings were rerented to others.

The Court: All right.

Mr. Chehock: Is there anything else you want?

Mr. Axelrad: This here.

Mr. Chehock: In regard to the minutes, what do you want to introduce?

Mr. Axelrad: I have here the copies of Artcraft Builders' minutes dated February 17, 1943, and August 18, 1942, which were marked, respectively, for identification Petitioners' Exhibit 22 and Petitioners' Exhibit 21. We spoke about it yesterday.

The Court: You are offering those?

Mr. Axelrad: I would like to offer those in evidence at this time.

The Court: Any objection?

Mr. Chehock: Well, you make the statement in the record that the originals of these particular minutes have been lost and that these are exact copies of the originals?

Mr. Axelrad: They are.

Mr. Chehock: No objection.

The Court: All right. They will be received and marked as Exhibits 21 and 22, the numbers by which they were [240] marked for identification.

(The documents heretofore marked Petitioners' Exhibits Nos. 21 and 22 were received in evidence.)

Mr. Chehock: Is that all?

Mr. Axelrad: That is all.

Mr. Chehock: What about these?

Mr. Axelrad: Do you want them marked for identification?

Mr. Chehock: Yes. Will you mark this for identification?

The Clerk: As a Respondent's exhibit?

Mr. Chehock: Yes, consisting of six sheets.

The Clerk: Respondent's VV for identification.

The Court: It may be so marked.

(The document above referred to was marked Respondent's Exhibit VV for identification.)

Mr. Chehock: Will Petitioners' counsel state what it wishes in regard to Exhibit VV?

Mr. Axelrad: Petitioners will stipulate that Respondent's proposed Exhibit VV is representative in form of the other 69 escrow papers relating to the sale of the 70 duplexes. The first document is a form of deposit receipt, in each case executed by Phil Boland, broker.

The second is a printed grant deed signed above the printed name, Edward Pool, Lottie Pool, William K. Murphy, [241] Edna Murphy, parties of the first part.

The third sheet is escrow instructions, the form prepared for this purpose by the Bank of America.

The fourth sheet is the Bank of America escrow statement showing the debits and credits at the end of the escrow.

The fifth document in this exhibit is a form of the letter written by Artcraft Builders, bearing the initials "R.W.," which is the secretary in the office of Artcraft Builders, to each tenant, notifying the tenant that the property had been sold and to pay the rent to the new purchaser, and stating who the purchaser is.

The last document in this exhibit is a form—there happened to be two tenants in the sale of this duplex, so there were two leases and they are identical.

Mr. Chehock: The Respondent offers Exhibit VV in evidence on the statement of Petitioners' counsel.

The Court: All right. It will be marked in evidence according to the number for identification.

(The document heretofore marked Respondent's Exhibit VV was received in evidence.)

Mr. Chehock: Now will you mark this?

The Clerk: It will be marked Respondent's Exhibit WW for identification.

(The document above referred to was marked Respondent's Exhibit WW for identification.)

Mr. Axelrad: Petitioners will stipulate, at Respondent's request, that Respondent's Exhibit WW is representative of the papers contained in each of the escrows relating to the 100 duplexes. The first document in this exhibit is a deposit receipt signed by Phil Boland, broker, who also signed the other 99. The form of the deposit receipt varied somewhat because it was on a different printed form, but it apparently had no substance as far as any issue in this case is concerned.

The second document is a grant deed relating specifically to the Tract 13163, in which the 100 duplexes were built and so printed in this deed. It bore the signatures of each of the associates over a space on which their printed name appears.

The third document is the escrow instruction form of the Bank of America.

The fourth document is a copy of a letter signed and apparently written by Phil Boland, addressed to the purchasers in each case, relating to the

processing of the loan, telling them what papers to bring with them, and not to come on Sunday.

The fifth document is a form letter bearing the name Artcraft Builders, signed by someone in that organization, written and addressed in each case to the then existing tenant, telling him or her that the property had been [243] sold and, after a certain date, to pay the rent to the new purchaser.

The sixth document is an identical letter, apparently, to the other tenant in that particular property.

The last is a letter by Artcraft Builders to the new purchasers stating that they were that day ordering a final reading on the water meter and notifying them that they should contact the Water Department to make arrangements for continuation of service and refunding a key deposit in the amount of $3.00.

Mr. Chehock: Respondent offers into evidence Exhibit WW on the statement of Petitioners' counsel.

The Court: It will be received and so marked.

(The document heretofore marked Respondent's Exhibit WW was received in evidence.)

Mr. Chehock: Will Petitioners' counsel stipulate that Lot 12 in Tract 11451——

Mr. Axelrad: That is the 70 duplexes?

Mr. Chehock: The 70 duplexes.—is a printed form deed under date of May 28, 1946? By "printed" I mean it prints the Tract No. 11451 and bears the date of May 28, 1946.

Mr. Axelrad: This is already in evidence?

Mr. Chehock: No, it is not in evidence, but rather than put it in evidence, I wonder if you would [244] stipulate to that?

Mr. Axelrad: We have one here.

Mr. Chehock: That is a later date and I want to get the date of May 28th in there, instead of June 4, 1946.

Mr. Axelrad: This is representative of all the deeds, we said.

Mr. Chehock: I want to show there is an earlier date on some of these form deeds on the 70 duplexes. One of them was made May 28th of 1946. Will you so stipulate?

Mr. Axelrad: So stipulated.

The Court: All right. The record will show that stipulation.

Mr. Chehock: Will you mark this for identification?

The Court: It may be marked Respondent's Exhibit XX for identification.

(The document above referred to was marked Respondent's Exhibit XX for identification.)

Mr. Chehock: I have had marked Exhibit XX, which is a Veterans Administration appraisal report taken out of the files, for Lot 60 on Tract 13163, to which is attached two pictures of the house and the various specifications of the house as set forth in the report.

Is that a correct statement, counsel?

Mr. Axelrad: You are not offering this as representative of all of them, but this particular one?

Mr. Chehock: Well, I am offering it as representative of the 100 duplexes.

Mr. Axelrad: You mean the pictures?

Mr. Chehock: The pictures and the specifications.

Mr. Axelrad: We will stipulate subject to this reservation, that they had different elevations; that is to say, this is representative of the general type, but they were not identical.

Mr. Chehock: Right. Good enough.

The Court: All right.

Mr. Chehock: The Respondent offers in evidence Exhibit XX.

The Court: It will be received and so marked.

(The document heretofore marked Respondent's Exhibit XX was received in evidence.)

Mr. Chehock: As previously stated, Petitioners' counsel and I have agreed it will not be necessary to take to court the original newspapers and someone from the paper to identify them as being original papers, but photostats would constitute a proper substitute.

I would like to offer in evidence as this time the affidavit of publication signed by W. H. Bradshaw for the Los Angeles Times, and two photostats of ads that appeared in their paper under date of August 11, 1946, and September 22, 1946, as indicative of the ads that appeared [246] on all the dates stated in the affidavit of publication.

The Court: Very well.

Mr. Chehock: Is that all right, counsel?

Mr. Axelrad: So stipulated.

The Court: They will be received and marked the next exhibit.

The Clerk: Respondent's Exhibit YY.

(The documents above referred to were received in evidence and marked Respondent's Exhibit YY.)

Mr. Chehock: I would like to state further that these other photostats that I am submitting to the Court here are advertisements which appear on a smaller sheet, but these were taken from the Public Library and they actually have been made smaller than in the papers. The papers are the regular size papers, the same as the Los Angeles Times.

The Respondent would like to offer in evidence at this time pages A-8 and A-9, two separate photostats, under date of August 10, 1946, of the Los Angeles Herald-Express; on A-8 of which appears a short write-up on the midde of the top of the page about the Artcraft Builders, Inc. homes being sold, and on the page A-9 appears an ad of the Artcraft Builders, "For sale, 50 duplexes."

Mr. Axelrad: Your Honor, on these write-ups, I don't know for what purpose they are being offered. They [247] purport to be little mast news items. I don't think the suggestion is made that Mr. Pool or Mr. Murphy wrote them or even that Artcraft wrote them.

I suggest, without further identification of their source they are not very well oriented in this record to any issue we have. I don't object to their going in. In other words, I don't contest the fact that they appeared in the newspapers.

The Court: You recognize that they were articles which did appear in the papers?

Mr. Axelrad: That is correct.

The Court: Well, that is really and truly what they are. They represent somebody's idea and somebody's article. I am going to let them in and you can make your argument.

I may say right now on this whole matter, I want to thank counsel for getting together and smoothing these things in. I think it is going to make an easier record to work with from the standpoint of all three of us, the Court and the parties. Of course, their being in and the fact that they come in by stipulation does not preclude either party from arguing as to the weight, or that the purport of what they appear to be has been rebutted by other evidence in the record.

Mr. Axelrad: Thank you, your Honor. [248]

The Court: They are received, and the two sheets will be marked as the Respondent's next exhibit.

The Clerk: Respondent's Exhibit ZZ.

(The documents above referred to were received in evidence and marked Respondent's Exhibit ZZ.)

Mr. Chehock: Respondent offers in evidence as the next exhibit, which would be Exhibit AAA—is that right?

The Clerk: That is right.

Mr. Chehock: ——two photostats, pages A-6 and A-7 of the Los Angeles Herald-Express of August 31, 1946, upon which appears, on page 6, an adver-

tisement: "We are selling 27 duplexes by the Artcraft Builders, Inc."

And on the page A-7 appears an article in the upper left-hand side about the sales.

The Court: All right. On the same basis, this will be received and marked as Respondent's Exhibit AAA.

(The documents above referred to were received in evidence and marked Respondent's Exhibit AAA.)

Mr. Chehock: The advertisements just offered have reference to the 100 duplexes.

I will now tender some advertisements in regard to the 70 duplexes. I offer in evidence as Exhibit BBB page 7 of the Los Angeles Herald-Express of May 4, 1946, on which appears an ad by the Artcraft Builders, Inc., stating, "For sale, 10 duplexes by the builders. Price $11,800." [249]

The Court: On the same basis, they will be received and marked as the next exhibit.

The Clerk: BBB.

(The documents above referred to were received in evidence and marked Respondent's Exhibit BBB.)

Mr. Chehock: Respondent offers in evidence page A-6 of the Los Angeles Herald-Express of May 11, 1946, as Exhibit CCC, on which page appears an ad of the Arteraft Builders, "For sale, duplexes, by the builders. Price $11,800."

The Court: It may be received and so marked as Exhibit CCC.

(The document above referred to was re-

ceived in evidence and marked Respondent's Exhibit CCC.)

Mr. Chehock: Respondent offers in evidence as Exhibit DDD an advertisement that appeared on page A-6 of the Los Angeles Herald-Express of May 18, 1946, which ad states, "For sale, duplexes, by the builders," and other representations.

The Court: It will be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit DDD.)

Mr. Chehock: Respondent offers in evidence as Exhibit EEE an advertisement appearing in the Los Angeles Examiner of May 19, 1946, on which, in the middle page, [250] appears an ad, "Artcraft Builders, Inc., for sale, duplexes."

The Court: That will be received and so marked.

(The document above referred to was received in evidence and marked Respondent's Exhibit EEE.)

Mr. Chehock: There is one that I failed to put in in regard to the 100 houses, that I would like to also tender at this time; pages Part I 10 and Part I 11 of the Los Angeles Examiner, September 1, 1946, page 10 of which includes an ad of Artcraft stating, "We are selling 27 duplexes for $13,000," and page 11 of which has a short article about it up in the upper right-hand corner of the page.

The Court: It will be received and marked as the next exhibit.

The Clerk: Respondent's Exhibit FFF.

(The documents above referred to were re-

ceived in evidence and marked Respondent's Exhibit FFF.)

The Court: All right. Mr. Murphy, will you take the stand again? [251]

Whereupon,

WILLIAM K. MURPHY

called as a witness for and on behalf of the Petitioners, having been previously duly sworn, resumed the stand and testified further as follows:

Cross Examination—(Continued)

Q. (By Mr. Chehock): Mr. Murphy, I refer you to the escrow paper which is sheet 3 of Exhibit WW, and you will note below the typing where William K. Murphy and Edna Murphy, Edward Pool and Lottie Pool appears, there is typed, "Signing date 9-23-46."

Do you know when that date was put on there?

A. It was put on there—no, I don't know the date it was put on. I presume it was put on 9-23-46. That's what it says.

Q. Did you have anything to do with putting it on there?

A. Not that I recall, no, sir. I don't remember. I don't recall if I did.

Q. Can you state, to the best of your recollection, when you were away from here, in the vicinity of these tracts, the 70 and the 100, during the year 1946, you and Mr. Pool? I think you said something about you were away and he was away. Can you state, to the best of your recollection, when you were away? [252]

(Testimony of William K. Murphy.)

A. Well, I checked last night with my wife and I was wrong about when I was away in my statement yesterday, that I was away until the 10th of September. I was in error. We got back on the 24th of August. I wanted to correct that.

Q. When did you leave and when did you come back? A. The 13th of August.

Q. You left on the 13th of August?

A. Yes.

Q. And you got back when?

A. We got back the 24th of August.

Q. So you got back on the 24th?

A. It was in 1947, that was the year we went fishing and were gone until September.

Q. Do you know, can you recall when you and Mr. Pool were away during 1946 at various times?

A. Well, it would be pretty hard to recall it. It is so far back. I know I was away fishing in May. I always go trout fishing in May. I know I was away in August trout fishing. That is the time this refers to. I know I went duck hunting at the opening of the season. Whether the season opened the 1st of October or the 17th of October, I don't know, that year.

The Court: Do they let you shoot duck out here in October?

The Witness: Yes. They used to. Last [253] year they opened the 17th of October.

The Court: What sort of duck do you get down here?

The Witness: We have a lodge up in Oregon.

(Testimony of William K. Murphy.)

We get mallards, honkers, and speckled breast geese.

Q. (By Mr. Chehock): When the 70 duplexes and the 100 duplexes were placed in escrow, what procedure did you, Mr. Pool, and your wives, use in signing the escrows for the Bank of America, the escrow agent?

A. As I stated yesterday, I don't remember whether they mailed them out to us or Boland brought them out. I know that we did sign them. As a matter of fact, I don't think they required all of our signatures on the original escrow. This is my recollection. I think they only required either Mr. Pool's or my signature. I don't think they required the four of us. Now, that is my recollection.

Q. Did you sign them the day that they were put in escrow or did someone sign for the four of you on that date?

A. Are you talking about the deed or the escrow?

Q. The escrow instructions to the Bank of America. I am talking about——

A. Well, they made those——

Q. I am talking about sheet 3, as an example, of Exhibit WW, which is entitled "Escrow Instructions," and which was signed for you four. [254]

A. This escrow instruction is dated August 20, 1946. There is no way of knowing when we signed it. I know to a certainty we didn't sign it on August 20, 1946. I am positive of that.

Mr. Chehock: I think we have stipulated, counsel, for instance, as an example, that this was placed

(Testimony of William K. Murphy.)

in escrow on August 20, 1946. I don't know if that coincides with the statement here or not.

The Court: Well, he is talking about the date of signing.

The Witness: That is what he asked me.

Mr. Axelrad: What we have stipulated in Exhibit O-15 and N-14, attached to the Stipulation in the case of each sale of the 70 and the 100 duplexes, is the date of escrow instructions, date of closing of escrow, date of grant deed, date of letters to the buyer and to the tenant, date of deposit receipt, and the number of the escrow at the Long Beach Bank of America main office.

Mr. Chehock: Fixing the date of the escrow instructions, wouldn't that be the date it was signed?

Mr. Axelrad: I don't know.

The Court: Let me see the exhibit. What paragraph of the Stipulation does it relate to?

Mr. Chehock: Exhibit N-14 and Exhibit O-15.

The Court: N-15 and O-15. All right. The [255] Stipulations says, Paragraph 22, the 70 duplexes in Tract 11451 were sold in 1946, as shown by Exhibit N-14 attached hereto and made a part hereof.

The 100 duplexes in Tract 13163 were sold in 1946 and 1947, as shown by Exhibit O-15 attached hereto and made a part hereof.

Now, on these exhibits we have various columns. The heading of N-14, the whole exhibit, says "Edward Pool & Associates, Detail of Sale, Year Ending January 31, 1947, Tract 11451, Duplexes." The first column, of course, is lot number. The second

(Testimony of William K. Murphy.)

column is tenant's name and address at time notice was sent. The third column is buyer's name and address at time escrow opened.

Then we have two columns under the general heading, "Escrow Date"; one of them being date of escrow instructions, and the other one, escrow close.

Now, counsel has asked this Petitioner about the signing of the escrow instructions, as I understand it, the date of signing with respect to the date shown on the papers, which I presume and which I would regard as being the dates on this Exhibit N-14 and the corresponding column on O-15.

Now, I don't understand, I wouldn't read this stipulation and this exhibit as saying that they necesssarily meant that the actual signing took place on that same day. I think it might be possible it did and it might be possible [256] it didn't.

I think now is a good time to let counsel know that I wouldn't regard the date in this column as necesarily being the date of the physical signing. I would regard that as indicating the date that was given as to effect and when it would be effective. That is the way I would read this stipulation.

I say that so that if there is any question about it and anything to be developed further along that line, you may be advised of the way I read that stipulation now while we are all here.

Q. (By Mr. Chehock): Is there anyone here that is appearing as a witness that would have knowledge of that?

(Testimony of William K. Murphy.)

A. I have a knowledge of it.

Q. When was it? What is your knowledge? What is your recollection?

A. I told you we absolutely did not sign it the date the escrow instructions were dated. I am positive.

Q. That is a negative. When was it signed?

A. That I can't tell you. You have got 170 escrow instructions there and I just don't have that good a mind.

The Court: Let me ask you this question, then, and maybe it will help out.

In one group there are 70, as I understand [257] it, and in the other group there are 100. In that column on the exhibit here, which I would say undoubtedly shows the date which appears on the document itself, and that date is opposite each individual lot, those dates vary. For instance on the first sheet of Exhibit N-14, which has to do with the 70— doesn't it?

Mr. Axelrad: That is right, your Honor.

The Court: On that first sheet, which runs through 11 lots, I see various dates, May 24, 1946, some in June, and one, the latest one was July 30, 1946.

Would you say that regardless of those dates, which are the dates appearing on the escrow instructions, the actual signing occurred at various dates as those dates would show, or did you sign all of them in a block, or what?

The Witness: No, sir. They would bring them

(Testimony of William K. Murphy.)

out as the escrow was opened. They were either sent out by Mr. Boland or mailed out. In other words, the procedure on an escrow—I presume your Honor knows how they are handled.

The Court: I might know something about it, but if it is of importance in the case, the record better show what it is.

The Witness: We dictated the escrow instructions.

The Court: You did what?

The Witness: Dictated the escrow instructions.

The Court: When do you do that in the [258] course of a sale?

The Witness: The real estate broker would take the party in that he is selling the house to and he would dictate his terms. The seller would go in and dictate his terms.

The Court: Yes.

The Witness: That is drawn up by the bank, typewritten, and usually mailed out to the buyer and to the seller for their signature.

The Court: That is, from the bank?

The Witness: That is from the bank.

The Court: After the bank has title to it?

The Witness: Yes.

The Court: Then what?

The Witness: Then they usually sign it, if it is agreeable to them, and they mail it back.

The Court: Then it is returned to the bank?

The Witness: Yes, sir.

The Court: In the normal course it could prob-

(Testimony of William K. Murphy.)

ably be, if both acted with dispatch, it would be a matter of mailing it out and mailing back, physically signing it and getting it back.

The Witness: Yes. In the event there was no difficulty, it would be in a few days. If the buyer had to qualify certain things or the seller did, [259] they may have held it up.

The Court: Now, what would be the basis, then, for the date that would be given the instructions? Who would fix that and at what time would the date be fixed that would go on it?

The Witness: The real estate broker or whoever opened the escrow. The date he dictated the instructions to the escrow officer is the date the instructions would carry. It may be that they weren't signed then, or a day or a month later.

The Court: They might be signed after?

The Witness: Definitely in this case they were signed after. I am positive of that. The fact of the matter is we submitted one escrow which he has got in the exhibits there, which is dated September 1, 1946.

The Court: Does that help us any, Mr. Chehock, or do you have something further?

Mr. Chehock: I think that helps. I think in the ordinary course of business they would be probably signed, if not that day, the next day or the following day.

Q. (By Mr. Chehock): Isn't that correct?

A. No, that isn't correct. I didn't mean to infer that at all. I said I didn't know when they were

(Testimony of William K. Murphy.)

signed, but I know they weren't signed the day that they were written. [260] They may have been signed the next day, they may have been signed the next week. I don't know when they were signed.

The Court: Unless some difficulty would arise, as a general matter, they would proceed with some ordinary dispatch?

The Witness: I have ten escrow instructions on my desk at my office on lots I am purchasing at the present time in San Pedro, and they have been on my secretary's desk at least two weeks. That is the dispatch I operate with.

The Court: You mean even though there is no question?

The Witness: No question at all.

The Court: No question about it and you just—

The Witness: They just sit there.

The Court: You are a procrastinator.

The Witness: Well, I guess I am.

The Court: I am, too, at times.

Q. (By Mr. Chehock): You wouldn't sign the escrow instructions until you would—I mean, you would have signed the escrow instructions prior to execution of the grant deed, wouldn't you, to the prospective buyer? A. Yes.

Q. What procedure did you, Mr. Pool and your wives follow in signing grant deeds both for the 70 duplexes and [261] the 100 duplexes?

A. Well, my candid opinion—and this is just my recollection—is that they were all signed at one time, except one signature, and I think if you will

(Testimony of William K. Murphy.)

refer to the one you have in the exhibit there, the one in the files there, I think you will find that is correct. That is the copy. There were three signatures on there and one signature was off so that nobody could use the deed. But they were signed in blank, all of them; that is my recollection.

Q. And then when was the fourth signature put on it?

A. The day that they were going to execute the deed.

The Court: Would that generally, then, be the date appearing on these sheets under the heading of "Grant Deed, Dated"?

The Witness: Yes, sir.

The Court: And generally that fourth name would go on on that date?

The Witness: The last name, yes, sir.

The Court: All right.

Q. (By Mr. Chehock): I tried to ask you a question yesterday and I don't think I succeeded in asking it of you very intelligently, but before I do ask it again, I am going to premise it by a little explanation.

By referring to Exhibit N-14 and [262] Exhibit O-15, first, Exhibit N-14, you will note that the date of escrow instructions and the grant deed dated, in most situations, not all, but in the great majority of cases, are within a few days of each other. Just examine Exhibit N-14.

A. What do you mean by a few days, now?

Q. Well, here is Lot 1, for instance, on Tract

(Testimony of William K. Murphy.)

11451, which was put in escrow May 24, 1946, deed dated May 28th, four days later.

A. This was sold to a party living there.

Q. Lot 2 was put in escrow July 29, 1946, and the grant deed was dated August 2, 1946; right?

A. Yes, sir.

Q. And so on down the line. The great majority of them were placed in escrow within a few days of the time the grant deed was made.

A. Well, this one is 20 days' difference. Another one is 20 days' difference. I would say the majority of them by far were within a few days after the escrow instructions were opened up.

The Court: All right. Now, what is your question?

Q. (By Mr. Chehock): Now, I refer you to Exhibit O-15 and ask you if that isn't generally true, with the exception of those that were placed in escrow in August of 1946.

A. Well, here is one in August that is six [263] months later.

Q. I am asking you first about those other than those that were put in escrow in August.

A. Oh, other than those in August. Well, here is one the escrow instructions are dated November 14, 1946, and the grant deed is dated October 17, 1946. The grant deed was made out before the escrow instructions. I don't know that this is even correct.

Here is one that is 22 days later. There is one that is 30 days later. Here is one that is 22 days later. Here is one that is 25 days later.

(Testimony of William K. Murphy.)

Q. That is one in August.

A. Oh, excuse me. Here is one that is 26 days later.

Q. Where? A. Right here.

Q. Right.

A. That is six off that page of about nine. Some of them are August, incidentally. Here is one 14 days later. Here is one 21 or 22 days later. That is August. 21 days later. There is one that is about 20—no, that is 40 days later. Here is one that is 47 days later. There is one that is 20, and there is one, 18. There is one, 20. There is one, 20. There is one, 30, There is one, 34—no, excuse me. That is 14. 17. 16.

There is one the escr : instructions are [264] again made out before the grant deed is made out; something wrong with that.

Q. Would you say from your examination that a majority of them are within a few days of the date they were placed in escrow?

A. Well, I called off the ones on there—I excluded any in August and I called off the ones that substantially quite a bit of time elapsed.

Q. With that explanation, let me ask you this question, Mr. Murphy: Do you know, Mr. Murphy, why the deeds for the lots in Tract 13163 that were placed in escrow in August 1946 were all dated subsequent to September 21, 1946, without exception, while the great majority or at least a great number of the deeds for the other lots, both for the 70 duplexes and the 100 duplexes, other than those

(Testimony of William K. Murphy.)

made in August 1946, were dated within a few days of the date the particular lots were placed in escrow? Do you understand the question?

A. Yes. May I ask when the first escrow was opened? What is the date of it?

The Court: 8-14.

Q. (By Mr. Chehock): 8-14, I think, 1946.

A. Well, it would be after that time the deeds would be drawn up by legal counsel, if such were the case, and they would also have to be printed, and after refreshing my memory [265] on the 70 duplexes, all of those lots were sold to the Bank of America.

On the 100 units there was some difficulty in financing the building, and the Bank of America finally refused to take them. All they would accept were those that were sold for cash.

I imagine there was a period in there of three or four weeks or maybe six or eight weeks that was required in order to finance them with the Mutual Funds Mortgage Insurance Company. I think if you will refer to the record, you will find out that statement is correct.

Q. Are you talking about being the escrow agent or the financing of the loans, or what?

A. I am answering the question. You asked me why the first deeds of the houses that were sold in August, we waited until September or subsequent to September 21st to execute the deeds.

Q. Right. A. And I told you why.

Q. I didn't quite understand it.

(Testimony of William K. Murphy.)

A. The 70 houses were all financed under the agreement by the Bank of America, that is, the 70. The 100, we thought they would take the same deal, and it is my understanding—not only my understanding, but even after refreshing my memory, the Bank of America after [266] the first lots were put in the Bank of America, they refused to take them.

The Court: What do you mean, the "first lots were put in"?

The Witness: The first sales in August.

The Court: You say that they——

The Witness: The Bank of America wouldn't finance them.

The Court: They wouldn't advance the money on them?

The Witness: Well, they didn't advance any money, your Honor. We sold them, we will say, to John Jones, and we assumed the Bank of America would make the same loan, of course, accept the same arrangement they had on the 70. They hadn't advised us to the contrary. The first batch of lots that were sold and went in there, after they were in there a few days, we were notified they wouldn't make the loans.

The Court: That is, the papers and the applications were there?

The Witness: That is correct. They would handle the escrow, but they would not make the loans. As a consequence, it was necessary to seek new financing. That is the first tract, to my knowledge, and

(Testimony of William K. Murphy.)

to the bank's knowledge, and anybody I know that is in the finance business out here, [267] that was ever financed where the building was sold, two units to two veterans, each owning half of the building. There was a period of three or four or five weeks that was necessary to work out the financing.

The Court: What was done in that period?

The Witness: In that period I personally contacted the Western Federal Savings and Loan, and my recollection was they said if we were selling the buildings, that they were going to sell our loans off. Then other lending institutions were contacted. I am speaking of the ones I specifically remember.

Then the Mutual Funds Mortgage Insurance Company was contacted, which represents, I think the name of the insurance company is the Massachusetts Mutual of Boston, or somewhere in Massachusetts. They were of the opinion that they could finance it, and it was necessary that they send the papers, or a dummy, as we call it, a typical setup, back with their appraisal, back to Massachusetts, in order to get their approval. The money came from the East. It did not come from out here. I think there was a period of four or five or maybe six weeks there before they could get it straightened out.

The Court: All right. Any further questions?

Q. (By Mr. Chehock): You have reference to financing, you have reference [268] to the purchasers getting financing to buy them, is that what you mean? A. That is correct.

(Testimony of William K. Murphy.)

Q. Most of these were sold to veterans, weren't they? A. That is correct.

Q. Weren't they GI loans that were guaranteed up to 100 per cent?

A. They guaranteed the loan or loans, but that don't mean you can go out and privately finance them. In other words, at that time and subsequent to that time I know of many, many occasions and times where you couldn't get GI financing, for the simple reason it was only four per cent. I know at that time I personally looked quite a bit myself for financing and finally arranged for it in the East. I would say most of them were financed by the Massachusetts Mutual Life Insurance Company.

The Court: Let me ask you here, on this so-called GI financing, is that in one respect comparable to these Federal Housing loans where the money is borrowed from private interests but insured or guaranteed by the federal agency, and in order to do so, the lender had to lend on certain prescribed conditions and at certain rates of interest, things of that kind?

The Witness: No, sir, it was not similar to the FHA. [269]

The Court: In the respects I mentioned?

The Witness: Well, no, sir.

The Court: All right.

The Witness: The FHA was insuring the loan 100 per cent and the GI loan was only insured for $4,000.00.

The Court: I am not talking about the insurance

(Testimony of William K. Murphy.)

particularly. I am not particularly interested in that. I am interested more in where the loan was made. It was made in each instance by outside parties, wasn't it?

The Witness: That is correct, yes, sir.

The Court: In order to come within the scope of whether it was GI or whether it was FHA, the loans had to be made according to whatever the conditions were that were prescribed by that agency?

The Witness: That is correct.

The Court: Did that include in each instance some restriction as to interest?

The Witness: Well, the interest was four per cent, and the amount of their loan, they would only guarantee up to $4,000.00.

The Court: All right.

Q. (By Mr. Chehock): What would the financing on the part of the buyer have to do with your signing a deed and putting it in escrow? If they didn't meet the terms of the escrow, [270] you would get your deed back, wouldn't you?

A. You wouldn't make out a deed unless you knew it was financed. At least, I wouldn't do it. In other words, they were entirely relying upon us. In the escrow instructions, where it was sold to a GI, it was sold subject to a GI loan. In other days the GI loans had just started and we were as much in the dark, at least I was, as the average GI that was trying to get one.

Then, as I said, there was an interim there of four to six weeks when there wasn't any financing,

(Testimony of William K. Murphy.)

and in my opinion that is why the deed usually issued on September 21st or subsequent thereto.

The Court: We will take an intermission at this time.

(Short recess taken.)

The Court: On the record.

Q. (By Mr. Chehock): I hand you a card that appears in this file for Lot 4, Block 1, Tract 13163, and will you state if you know anything about those cards?

A. No, sir. I never had anything to do with drawing them up.

Q. Those cards there indicate in pencil, on Lot 4, that there was no lease on either of the properties there.

A. That is correct. I think that is true, because [271] this is in Mrs. Woodruff's writing.

Q. It is in her writing? A. Yes.

Q. And Mrs. Woodruff was an employee of Artcraft and Edward Pool & Associates?

A. Yes. She is here in court.

Q. We have stipulated, and I think maybe you have already testified, that Artcraft handled the rentals for Edward Pool & Associates, didn't they?

A. Yes, sir.

Q. During all this period? A. All the time.

Q. And Boland handled the sales for Edward Pool & Associates by use of the name of Artcraft; is that right?

A. Well, he handled the sales for Edward Pool & Associates.

(Testimony of William K. Murphy.)

Q. And used the name of Artcraft, as these ads show? A. Yes, that is correct.

Q. Would you say Edward Pool & Associates was in the rental business?

A. I wouldn't answer that. I don't think I am qualified to answer. I don't know.

Q. In what business would you say Edward Pool & Associates was?

A. As I said before, I don't know. We had apartment [272] buildings down there that I thought we had as an investment, that we were keeping for an income.

Q. If Edward Pool & Associates was in the rental business, wouldn't they also be in the house selling business?

A. Edward Pool, to my knowledge, never sold any houses.

Q. They didn't handle the rental, did they?

A. Artcraft Builders maintained the properties for Mr. Pool, Mrs. Pool, myself and my wife, and collected the rents and did what was necessary to keep them up and keep the properties in good shape.

Q. What I am saying is this: Since Artcraft handled Edward Pool & Associates' rental business, they handled that the same as Boland handled the sales business of Edward Pool & Associates, didn't they?

Mr. Axelrad: I would like to object on the ground the question is argumentative. The witness said he couldn't answer whether he was in the rental business. I think he was suggesting, as I think it is,

(Testimony of William K. Murphy.)

that it is a legal conclusion. Now he is premising his next question on the assumption the witness has stated, which he has not, that he was in the rental business.

The Court: I think there is something to that. You will present your evidence here as to what was done, and these questions now generally go to the question that [273] I will have to decide, which does have a legal import.

Mr. Chehock: You are right, your Honor.

The Court: That is as to whether or not it is within the meaning of the statute, whether what was done is within the meaning of the statute. I will have to decide that on the basis of these operations and the picture I get when it is all pieced together.

Mr. Chehock: That is all.

The Court: Anything further?

Mr. Axelrad: Your Honor, I have a number of questions which I would like to ask Mr. Murphy, but there is a witness who has been waiting, who will take only five or ten minutes. He has been here a long time. He has important business this afternoon, and I wonder if we might take him now.

The Court: How long do you think you will take with Mr. Murphy?

Mr. Axelrad: Well, I would think it would take probably 20 or 30 minutes or maybe longer.

The Court: I guess we have had interruptions before and I don't suppose this will make any material difference, unless counsel has some feeling on it.

Mr. Chehock: I have no objection.

The Court: All right. You may step down, sir.

(Witness temporarily excused.) [274]

Whereupon,

CYRUS EDWARD LA BREE,

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your full name for the record, please?

The Witness: My full name is Cyrus Edward Le Bree, L-a B-r-e-e.

Direct Examination

Q. (By Mr. Axelrad): Mr. La Bree, what is your occupation?

A. At the present time I am associated with a real estate loan broker.

Q. What generally has been your business or professional experience, say, from 1940 onward?

A. From 1940 on I was with the Bank of America and the Farmers Bank of Watts.

Q. What were your duties with the Bank of America? A. I was assistant cashier.

Q. In connection with those duties, did you ever meet one of the Petitioners in this case, Mr. Murphy?

A. Along toward the end, the latter of 1941, I met Mr. Murphy at the Bank of America Florence Branch.

(Testimony of Cyrus Edward La Bree.)

Q. Under what circumstances, what was Mr. Murphy [275] seeking or why was he there?

A. He was in there at that time on behalf of Arteraft Builders making application for 143 Title 6 loans to be constructed, the houses to be constructed in Long Beach.

The Court: What do you mean when you say "Title 6 loans?"

The Witness: At that time there was a new title come out——

The Court: Title of what?

The Witness: Under the FHA, under the Federal Housing Administration Act, a new title was out to assist building homes for people working in defense plants.

The Court: All right.

Q. (By Mr. Axelrad): Title 6 was a type of financing that the Government had something to do with?

A. Yes. It was a loan which they guaranteed 90 per cent under the Act.

Q. Did you assist Mr. Murphy through the Bank of America, on behalf of the Bank of America, I should say, in making this loan?

A. We were finally able to work it out along in February, in the month of March, 1942, and I worked with them and assisted him and Mr. Pool in the association of Arteraft Builders. [276]

Q. What kind of buildings were these that were being financed, do you recall?

A. The 143 were single-family dwellings.

(Testimony of Cyrus Edward La Bree.)

Q. What was your next contact with Mr. Murphy?

A. Along in the fall, it was, I believe, in August or September of 1942, he discussed with me the possibilities of some more financing down there. At that time they were not going to be single-family dwellings. They were going to be larger units at that time, duplexes.

Q. Did they discuss with you or did you have any reason to inquire why they were going to build duplexes instead of single-family units?

A. At that time in that area housing was very scarce and there was a large demand for some place for the defense workers to stay and not have to own their property, to rent.

Q. But the question was why. Did they say why, or do you know why they were going to build duplexes?

Mr. Chehock: I object to this as hearsay.

The Court: He said "do you know."

The Witness: My answer to that would be that I had discussed with them some time before that the reason was that inasmuch as we had had so much demand in that area for housing accommodations, that it might be wise to construct some units and have them for their own. [277]

Q. (By Mr. Axelrad): You mean your testimony is that you suggested to them——

A. I had spoken to Mr. Murphy several times when I was down there.

Q. This was before they came in and made ap-

(Testimony of Cyrus Edward La Bree.)

plication for financing, or did they make application for financing?

A. I would say it was along about the same time, along in August, if I recall.

Q. August of what year? A. 1942.

Q. What was Mr. Murphy's reaction to this suggestion? Was it Mr. Murphy?

A. Yes. I had talked to Mr. Murphy about that.

Q. Did you ever talk to Mr. Pool about it?

A. Yes, I discussed it with Mr. Pool, if my memory serves me correct. The reaction was they were going to go ahead on their individual housings for a while.

Q. Did the subject come up again?

A. Yes, it did. Later on it come up again and they were going to go in and build these units that I spoke about, the duplexes. The number of them I don't recall. But I do remember that in one conversation we had, that the units were going to be constructed and they were going to be held by them.

Mr. Chehock: I move to strike that as hearsay, your Honor.

The Court: The motion will be denied.

Q. (By Mr. Axelrad): Did you ever have occasion to see the property that was built?

A. Oh, up until—I stayed with the Bank of America until the end of February, 1945, and I was probably down there at least every 15 days until that time.

Q. Why would you go down every 15 days?

A. Because we were interested in the financing

(Testimony of Cyrus Edward La Bree.)

of the houses. We were also interested to see how the houses were maintained, in view of the fact that we were carrying loans.

Q. How were they maintained?

A. Very satisfactorily.

Q. Was there any discussion with you in your capacity as a representative of the Bank of America as to whether they were going to sell these things? Were you interested in financing on a short-term basis or did the Bank of America treat this as a longer investment? A. We were in the——

The Court: I think at this point there isn't any showing that one would be short term and the other would be long term, necessarily. So I think the basis for your [279] question is not in the record.

Mr. Axelrad: Let me rephrase it, then, your Honor.

The Court: All right.

Q. (By Mr. Axelrad): Did the Bank of America finance any of these duplexes or apartments that have been discussed here today?

A. I am not able to answer that because, as I recall, I am just going from memory now, the office that I was in financed the 143 houses. I recall that some of the units—I am talking about the duplexes—were financed by a savings and loan association here in Los Angeles.

Q. You say you visited the property every few weeks. What property were you referring to?

A. I was interested in all of them, for the simple reason after we financed the 143 at the Florence

(Testimony of Cyrus Edward La Bree.)

Branch, one of the other offices of the Bank of America stepped in and wanted to take the thing over, with the result we lost all the financing and it went to a savings and loan.

Q. But you still continued to visit the property?

A. Sure; always hopeful we could some day get back in.

Q. Did you know Mr. Murphy and Mr. Pool apart from your business relations with them through the Bank of America?

A. Oh, yes, I knew them personally.

Q. Did they ever discuss with you any plans for disposition of these properties, ask your advice? [280]

A. Yes, they had, and my recommendation was that they hold this, the other units that they had built, because I knew Mr. Murphy, knew his family, and that was my thought.

Q. Did you know whether they ever sold these properties?

A. Well, I heard in the latter part of 1946 that they had, heard from——

Q. That they had what?

A. That they had sold some after I had left the Bank of America. I left the Bank of America and then went with Sawyer Cabinet, and while I was with Sawyer Cabinet, they were supplying cabinet work for the jobs that Mr. Murphy and Mr. Pool were constructing. I was there at various times then, and later I heard they sold them, were selling them. I saw mention of that for the first time in advertisements in the newspapers.

(Testimony of Cyrus Edward La Bree.)

Q. Were you surprised?

A. I was very much surprised.

Q. Was that consistent or inconsistent with their expressed plans?

Mr. Chehock: Your Honor, I think all this testimony is immaterial. Whether he was surprised, what has that got to do with it?

The Court: I agree with you on that. I don't [281] think it makes any difference whether he was surprised or not. Let's get along now.

Mr. Axelrad: I think it has this much to do with it, your Honor,——

The Court: Let's get along.

Mr. Axelrad: If it is all irrelevant, there is no use spending our time on it.

The Court: I am allowing you to go ahead. Counsel thinks it is relevant, so go ahead and put it in.

Q. (By Mr. Axelrad): You had been discussing financial questions with them from time to time over a period, I take it, from 1942 on up, is that correct?

A. From the start of 1942, yes, sir.

Q. But they hadn't discussed with you any plans to dispose of the property? A. At no time.

Q. The first time you knew of it was when you read it in the paper? A. Yes.

The Court: And that surprised him. Now, let's move along.

Mr. Axelrad: That is all.

The Court: Any questions?

Mr. Chehock: No questions. [282]

The Court: You are excused.

(Witness excused.)

Whereupon,

WILLIAM K. MURPHY

called as a witness for and on behalf of the Petitioners, having been previously duly sworn, resumed the stand and testified further as follows:

Redirect Examination

Q. (By Mr. Axelrad): Mr. Murphy, what has been the status of Arteraft Builders, Inc. since 1946, what has the corporation been doing, if anything?

A. Nothing. We haven't been doing anything.

Q. There was some testimony yesterday on cross examination concerning Arteraft Builders of New Mexico and Arteraft Builders of Colorado. Is that correct? A. Yes, sir.

Q. Did you and Mr. Pool and your respective wives own stock in those two corporations in the same proportion to your stock holdings in Arteraft Builders, Inc.?

A. Our wives never owned any stock in Arteraft Builders of New Mexico or Arteraft Builders, Inc. of Colorado.

Q. Did anyone else own stock in those two corporations?

A. Yes, sir. Mr. Pool and myself and Major General Patrick J. Hurley. [283]

Q. Did Major General Hurley own any stock in Arteraft Builders, Inc.? A. No, sir.

(Testimony of William K. Murphy.)

Q. Was there any connection of any kind between Artcraft Builders, Inc. and Artcraft Builders, Inc. of New Mexico? A. None whatever.

Q. Did they ever do business with each other?

A. No, sir.

Q. No tie-in of stock between them?

A. No, sir.

Q. Was there any connection between Artcraft Builders, Inc. and Artcraft Builders of Colorado?

A. No, sir.

Q. They never did business with each other of any kind? A. No, sir.

The Court: What difference does it make?

Mr. Axelrad: I think it makes this difference, your Honor. Mr. Chehock brought in activities of Artcraft Builders of New Mexico and Artcraft Builders of Colorado. I did not think it had any relevance, but I wanted it to be clear he is talking about corporations completely different than the one involved in this case.

The Court: I think the record already shows that. [284] I don't recall anything that said that they weren't separate. They did have to do with the activities of Mr. Murphy and Mr. Pool individually, and there was some testimony that they were interested in those corporations, those endeavors, but, as I understood it, it was possibly as officials and stockholders of those corporations, because I understood they were incorporated.

Mr. Axelrad: The record showed that and I wanted to show these additional things.

(Testimony of William K. Murphy.)

The Court: I don't think it is additional. I think it is just more of the same. But go ahead.

Q. (By Mr. Axelrad): What was your position with Arteraft Builders of New Mexico?

A. Secretary and treasurer.

Q. Were you paid a salary? A. Yes, sir.

Q. What was that salary?

A. $500.00 a week.

Q. What did you do?

A. I ran the office, handled the financing.

Q. What about Arteraft Builders of Colorado?

A. I was secretary and treasurer there.

Q. What did you do for them?

A. Same thing. [285]

Q. The same thing? A. Yes, sir.

Q. What did you get, the same salary?

A. No, sir.

Q. What did you get for a salary?

A. $750.00 a week.

Q. What about Mr. Pool? Was he employed by both? A. Yes, sir.

Q. In what capacity, what kind of work? I don't mean his title, but what did he do?

A. He done the building.

Q. Was he paid? A. Yes, sir.

Q. Do you know what his salary was?

A. $500.00 a week in Arteraft Builders of New Mexico, and $750.00 a week in Arteraft Builders of Colorado.

Q. There were other employees of both companies? A. Yes, sir.

(Testimony of William K. Murphy.)

Q. Did Arteraft Builders, Inc., the Petitioner in this case, in this series of cases, ever build anything which it sold to you or any of the other stockholders, which you then sold without holding?

A. I don't understand the question.

Q. Did Arteraft Builders, Inc. ever build any property which you bought or otherwise secured from it as individuals, [286] other than the properties which you had testified concerning in your previous testimony? A. No, sir.

Q. You testified yesterday, I believe, Mr. Murphy, that sometime in the spring of 1946, it became the policy of the associates not to take written leases on the duplex apartments, is that correct?

A. Yes, sir.

Q. And you stated the reason was that you hoped that rent control would go off.

A. That is correct.

Q. And why would a lease be disadvantageous to you in that event?

A. Well, our attorney told us it was not advantageous to us to have a lease in view of the fact that we couldn't collect the last month's rent in advance, and in view of the fact that rent control was on, we couldn't increase the rent.

I refreshed my memory last night and this morning with the records over there on the desk, and the last lease we made was April 13, 1946—it was April 10th, I think.

Q. What was the status of those tenants from

(Testimony of William K. Murphy.)

that point on when you didn't make the—strike that.

In the first place you did have leases after that time? A. Oh, yes. [287]

Q. In other words, some had been leased for periods beyond April, is that correct?

A. Oh, yes.

Q. It is only that when the leases expired, you didn't make any new ones from that date on.

A. Yes.

The Court: Let me ask you this: In the absence of rent controls, how would the having of a lease have any effect on increasing the rent?

The Witness: In the absence of rent control?

The Court: Yes. In other words, if you had a written lease, you normally fix the rent for the term of that lease and it wouldn't be subject to increase unless there was a provision in there to that effect, would it?

The Witness: 99 per cent of our duplexes, your Honor, had the husband and wife and at least one child, and in some instances, I testified yesterday there were nine living in the apartment. We didn't want leases because we were advised by our attorneys if the rent control was off, the lease was of no advantage to us, is what they told us.

The Court: I can see where it was no advantage insofar as raising the rent.

The Witness: It later developed on the buildings we did have leases, when rent control went off, we couldn't increase our rent. [288]

(Testimony of William K. Murphy.)

The Court: I can understand that.

The Witness: I presume that is what they had in mind.

The Court: I don't think you made that clear and that is what I wanted to know about. If you had a term lease and if that term lease said your rent was $100.00 a month, and at the end of six months rent control went off and the market would then have permitted normally an increase to $125.00, you would have been tied by your lease to $100.00 for the term unless you had an escape clause in the lease.

The Witness: We had some leases, I think, that had three months to run or all of the year to run except one day, and when they increased the rent, they made us write a new lease for in excess of the year.

Q. (By Mr. Axelrad): That was 1948, wasn't it? A. That is right.

Q. The amendments to the rent control law.

A. Yes.

The Court: That is when you were permitted to raise them?

The Witness: Yes.

The Court: Go ahead.

Q. (By Mr. Axelrad): Mr. Murphy, what was the situation in the spring [289] of 1946? Did you expect rent control might be eliminated? Were you hoping that it would be?

A. We hoped it would be, yes. We hoped it would be after the war was over, in fact.

(Testimony of William K. Murphy.)

Q. Were you advised leases would keep the rent lower in the event rent control went off?

A. We were advised by our attorney, Mr. Swaffield, after a conference with the OPA, that there was no advantage in having the lease, as I have testified. We were paying him a fee by the month, so we did what he told us to do.

Q. In response to Mr. Chehock's questioning yesterday you stated that the status of the tenancy after the elimination of leases beginning in April, 1946 was from month to month, is that correct?

A. The ones that didn't have a lease on. Of course, there were—I would say in April they were 99 per cent rented, to my recollection.

Q. You mean leased? A. That's right.

Q. By month-to-month tenancy, would you suggest that you had the right to put out, or do you know whether you had the right to put them out on 30 days' notice?

A. No, we did not have the right to put them out.

Q. Why not?

A. The OPA wouldn't let us. We tried to put some of [290] them out where there were three or four in the family, or where they had a dog.

Q. You testified yesterday, and the stipulation shows, that the 70 duplexes were sold some period before the 100. A. That is correct.

Q. You also testified that the reason you sold the 70 was that you felt there was a better place to put your money that you get from the sale of

(Testimony of William K. Murphy.)

them as far as a return from your investment was concerned, is that correct? A. Yes, sir.

Q. Then Mr. Chehock asked you why that didn't also apply to the 100. Can you suggest any reasons other than you gave yesterday relating to that? Why you would sell the 70 and keep the 100 for an additional period. Why didn't you sell all your real estate once you decided to sell the real estate?

A. I don't know what I could add to it. I told Mr. Chehock we didn't desire to sell all our holdings, that we intended to hold some for investment.

Q. Was that based on anything rational or on some notion that 70 was a magic number and ought to be sold, and 100 ought to be kept? Did you have any reason for it?

A. Well, I have had stocks and if I was liquidating I wouldn't necessarily liquidate everything I had because I wanted to sell something. We sold the 70 because Boland [291] prevailed on us, told us it was a good thing to sell, he could get the top market for us, and we sold them.

The 100, we had no desire to sell at that time, and the fact of the matter is when we started the 70, we never intended at any time to sell the 100 or the 22 apartments, either.

Q. Was there a question of diversity in your investment? A. That is correct, yes, sir.

Q. What does that term mean to you?

A. It means just what happened. I bought Guaranty Trust, United States Steel, Anaconda Copper, Chrysler, General Motors.

(Testimony of William K. Murphy.)

Q. You testified yesterday, or perhaps it was the day before, that if you had wanted to build something for sale, you would have built single-family units.

A. Yes, sir, that is what I would still do.

Q. Can you explain in any more detail why a single-family unit, in your opinion at least, is a better and a more salable property?

A. A single-family unit, it is my opinion that the American public, the American people want homes. They want something of their own. They want a yard for their kids to play in, instead of being cooped up in the apartment. The price of a single-family unit would be a lot less than a [292] duplex or a larger building, and it would be much easier to sell.

Q. Mr. Chehock read some advertisements to you, which apparently appeared in the newspapers in this vicinity. These advertisements made it seem very desirable to own duplexes. How do you explain that? Is that inconsistent with your statement that you think most people would rather own single-family residences?

A. Well, I didn't write the ads and I didn't approve them, and, as a consequence, why, what was put in the ads I wasn't consulted on. The fact of the matter is I don't think I saw half of the ads until Mr. Chehock showed them to me.

Q. There was a question asked you concerning whether Arteraft's offices also were the offices of Edward Pool & Associates. Were they?

(Testimony of William K. Murphy.)

A. Well, I did not know what you meant. I don't know what you mean by the question of both offices.

Q. Where is Artcraft's offices?

A. Artcraft's offices at that time, you mean?

Q. Yes. A. 2187 Lakewood Boulevard.

Q. Was there a sign on the door, the window, or anything else, indicating what it was?

A. A big neon sign and a painted sign on each window. [293]

Q. What does it say?

A. That is what it said, "Artcraft Builders, Inc."

Q. Does it say "Edward Pool & Associates?"

A. No, sir.

Q. Did the people in the apartments that were renting know anything about Edward Pool & Associates? A. No, sir, absolutely not.

Q. What exactly is that word, "Edward Pool & Associates?" I don't mean a legal conclusion. I mean, as a matter of fact, what did Edward Pool & Associates, as such, do, what was its purpose?

A. Edward Pool & Associates was Mr. Pool and Mrs. Pool, my wife and myself. We didn't do anything.

Q. Is it a correct statement that this was just a group of four people that had a joint investment?

A. That is correct.

Q. Is that absolutely all it ever did?

A. It is absolutely all it ever did.

(Testimony of William K. Murphy.)

Q. Did you have made out the partnership return in the name of Edward Pool & Associates?

A. I don't know. Oh, yes, income tax, yes, sir.

Q. Why did you do that?

A. I don't know. Our auditor made it out.

Q. You mean you were advised that is what was required? A. Yes, sir. [294]

Q. What was the exact relationship of Arteraft Builders, Inc. to the four of you that owned these apartments? What did Arteraft have to do with your investment or your activities—I am talking about the associates' activities—after you acquired title to the 70 duplexes, 100 duplexes and 22 apartments? A. They rented the buildings.

Q. Arteraft rented the buildings?

A. Yes, sir.

Q. Well, it is stipulated that was a rental agent.

A. Property management.

The Court: Hasn't this all been rather clearly covered?

Mr. Axelrad: I thought it got a little confused, your Honor, on cross examination, but maybe it did not. I wanted it to be crystal clear, if I could make it that way.

The Court: I think it is. Whatever Pool & Associates did, this witness testified, was done from those offices, and he rather in detail stated about what they did and that he personally didn't do anything except some formal acts, and that what records they had and books, and so forth, were kept

(Testimony of William K. Murphy.)

down there in the same place where Artcraft Builders was.

Q. (By Mr. Axelrad): Mr. Murphy, would it be possible or would it have [295] been possible, that is, for you as an investor and your associates, to have hired someone else to do what Artcraft did?

A. Oh, yes, it would have been. Lots of people would like to. We could have hired anybody. I imagine we could.

Q. You mean it is quite common for one corporation or entity to perform management services for buildings? A. Yes, sir.

Q. You know that such things are done.

A. Oh, yes.

The Court: There are people in that business. A lot of real estate offices act as rental agents. That is just form.

Mr. Axelrad: That is something you can take judicial notice of, I assume.

The Court: If I could do as the Fifth Circuit told me I should do, take judicial notice that the break in the Florida boom in land was in 1925, and under that a man could sustain a loss on a piece of real estate by going out and looking at it and saying he wouldn't have anything more to do with it, then I might be able to take note of commonly accepted business practices which might well be a matter of common sense.

Of course, I would rather imagine that back during [296] the war years and immediately following there, that it was not as easy to find people to do

(Testimony of William K. Murphy.)

things, even though they were in the business, because they didn't have time. They were already too busy. But that didn't make it any the less the fact that the business practice was well established, as we all know.

Q. (By Mr. Axelrad): Mr. Murphy, you testified that you, I think in your words, that you retired in 1945, is that correct? A. Yes, sir.

Q. What do you mean by that?

A. I quit work.

Q. You quit doing all work?

A. That is right.

Q. Why did you quit at that time?

A. Well, I figured I was going to live off of my investments.

Q. In other words, it was no longer necessary for you to earn a living? A. That is correct.

Q. And you had better things to do with your time? A. I thought I did.

Q. What did you do, assuming you were in town and not away fishing or hunting, which I assume you did something of, from your testimony, what did you customarily do [297] with your time during a business day, working day?

A. Well, get up in the morning at 6:00 o'clock and go over to E. F. Hutton & Company and stay over there until about noon.

Q. What is E. F. Hutton & Company?

A. Members of the New York Stock Exchange, brokers.

Q. They were stock brokers? A. Yes, sir.

(Testimony of William K. Murphy.)

Q. They were your stock brokers?

A. Yes, sir.

Q. And you had a lot of dealings with them?

A. Yes, sir.

Q. Then what would you do in the afternoon?

A. Well, sometimes I would go down to the club, sometimes I would play golf, sometimes I would go out pistol shooting with Mr. Pool.

Q. Did you ever go to the offices of Arteraft?

A. Once in a while, yes.

Q. Did you spend more time at the offices of Arteraft than you did in the offices of Hutton & Company, or vice versa, would you say?

A. Well, I don't know. I know I spent as much time in one place—I used to go down to the office once in a while and go in. I didn't do anything in particular.

Q. In Arteraft's offices? [298] A. Yes.

Q. Yesterday you testified that one of the reasons, or the principal reason that you and Pool bought out Cooke and Smith is because Cooke and Smith wouldn't agree to use the Arteraft as a vehicle for building duplexes and apartments that the stockholders might acquire, is that correct?

A. Yes, sir. They said that they didn't want anything to do with any apartment buildings.

Q. You also testified after this was brought to your attention, that applications for 22 apartments were filed while Cooke and Smith were still stockholders. A. 22, and also the 70 duplexes.

Q. Were there negotiations at that time for

(Testimony of William K. Murphy.)

buying out Cooke and Smith, or did you for the first time decide to buy them out on the date indicated by the minutes of the corporation, which are in evidence?

A. No. Negotiations started, I would say, quite a while previous to the actual time that the minutes show they resigned. As a matter of fact, the minutes—we had our attorney draw up the minutes whereby Mr. Smith and Mr. Cooke resigned, I think they are dated June 8, 1946, and also Mr. Cooke and Mr. Smith's resignations were drawn up, and when that meeting was called, Mr. Smith and Mr. Cooke had already agreed to the sale and we had paid them off prior to that time and they resigned.

Q. I hand you here Federal Housing Administration Subdivision Form. Can you indicate what this is?

A. That is an application for the approval of a subdivision on which 140 duplexes were to be built for rental.

Q. Mr. Chehock has called my attention to the fact that you have talked about June 8, 1946, in buying out Cooke and Smith. That was not the correct year, was it? A. 1943. I am sorry.

Q. Now, you say this is an application for a subdivision approval? A. Yes, sir.

Q. Which subdivision?

A. Well, that is a subdivision right north of Long Beach, in Compton.

Q. Is that the one that you testified to yesterday,

(Testimony of William K. Murphy.)

testified about yesterday when we had the plat, the subdivision plat?

A. Well, this one is in Compton. I don't remember whether I testified to it or not.

The Court: You testified about one that you later discovered was the subject of oil leases.

The Witness: Yes, this is the one. I remember now.

Q. (By Mr. Axelrad): What does that say about whether they are to be [300] held for sale or rental, if anything?

A. No. Number of homes to be built immediately to order, 280. Number for sale, none.

Q. What was the date of this, according to the paper? A. April 1, 1946.

Q. Was this actually filed, the original of this document actually filed with the Federal Housing Administration?

A. Yes, sir, and it was approved.

Q. Approved subsequent to this date?

A. Yes, sir.

Q. Do you know in a general way at what time, how long it would have taken?

A. Well, it takes different times, from a month to six weeks. I think that was approved in six weeks or eight weeks, something like that.

Q. That would be around the middle of May?

A. Yes.

Q. 1946? A. Yes.

Q. You said this was not built because of oil leases that existed? A. Yes, sir.

(Testimony of William K. Murphy.)

Mr. Axelrad: I would like to offer this subdivision information form as Petitioners' Exhibit No. 28. [301]

The Court: Any objection?

Mr. Chehock: No objection.

The Court: It will be received and so marked.

(The document above referred to was received in evidence and marked Petitioners' Exhibit No. 28.)

The Court: I think we are going to have to adjourn for lunch. How much more have you got?

Mr. Axelrad: Oh, I would say, I hesitate to say, but about five minutes, I will say.

The Court: I will run along for a few minutes. I would like to finish this witness, if we could.

Q. (By Mr. Axelrad): I hand you a copy of a letter purportedly written by Arteraft Builders, Inc., dated July 9, 1943. Can you identify the letter and say in a general way what it relates to?

Mr. Chehock: We have no objection to the letter going in, unless you want the witness to testify about it.

The Witness: This was a letter I wrote to the Douglas Aircraft Corporation at Long Beach and addressed to the attention of Mr. Lindberg, who was the head of the housing department, and told him we would have 208—198—no, 208 rental units for rent to the Douglas employees. We stated we would lease them to them for a period of the duration plus six months, if they desired leases, to the Douglas [302] Corporation.

(Testimony of William K. Murphy.)

Mr. Axelrad: I would like to offer this letter as Petitioners' Exhibit No. 29.

Mr. Chehock: No objection.

The Court: It may be received and so marked.

(The document above referred to was received in evidence and marked Petitioners' Exhibit No. 29.)

Q. (By Mr. Axelrad): By that letter did you mean that you would make a master lease of all your properties? I gather the 208 refers to the 140 duplexes.

A. The 140 duplexes and the 22 buildings, which consist of 68 units. That is 208.

Q. Was there the intention that this be a master lease to Douglas? A. That is correct.

Q. What was the result of that letter?

A. They didn't give us a master lease. They sent referrals down with referral slips for people to rent individually.

Q. Is it because they didn't want to take the responsibility as a company, or why was it?

A. They didn't say why. At least, I don't recall their saying why.

Mr. Axelrad: I would like to offer in evidence as [303] Petitioners' Exhibit 30, NHA General Order No. 60-3-C. For the Court's information, we have a number of these NHA amendments that relate to these war housing priorities in evidence as exhibits to the Stipulation, but this is is an additional one that I have found since. The ones we have in there are not complete, apparently. This

(Testimony of William K. Murphy.)

come directly from the Housing Authority in Washington, and I have one additional one.

The Court: Any objection?

Mr. Chehock: No objection.

The Court: It may be received and marked as the next exhibit, Petitioners' Exhibit 30.

(The document above referred to was received in evidence and marked Petitioners' Exhibit No. 30.)

Mr. Chehock: I assume we are going to furnish each other photostats of these different exhibits, aren't we, counsel?

Mr. Axelrad: I assume so.

The Court: I think we will adjourn for lunch and then conclude after lunch. You can have checked over your notes and determined what more you want of this witness by then.

Mr. Axelrad: On this question, your Honor, I have a number of additional amendments.

The Court: You won't need the witness for that?

Mr. Axelrad: On one of them, I do.

The Court: All right, get it in, then.

Mr. Axelrad: I just wondered if we wanted to put this in. They seem to duplicate each other and have just a few little changes.

The Court: You better go over them and clear them with counsel. If there are any questions about having a complete set of those things in there, whether the omission of some of them leaves gaps in the instructions and regulations, or whatever they are, you can check them and find out. Each

(Testimony of William K. Murphy.)

of you will have to determine the things on your own judgment.

We will come back at 2:00 o'clock.

(Whereupon, at 12:35 p.m., a recess was taken until 2:00 p.m. of the same day.) [305]

Afternoon Session

2:00 p.m.

Mr. Chehock: Your Honor, I have been contacting the Federal Housing Administration endeavoring to get some information on the lifting date on the selling price on these war houses.

It is my understanding, although I didn't get it from them, and I think counsel is willing to let it be so considered, that the lifting was made in October, 1945 by executive order.

Mr. Axelrad: By executive order.

Mr. Chehock: Yes.

The Court: All right. I had some recollection of some such date, but I didn't know for sure.

Whereupon,

WILLIAM K. MURPHY

called as a witness for and on behalf of the Petitioners, having been previously duly sworn, resumed the stand and testified further as follows:

Redirect Examination—(Continued)

Q. (By Mr. Axelrad): Mr. Murphy, I hand you a copy of Exhibit H-8-D, which is a National Housing Authority General Order No. 60-3-B. Were

(Testimony of William K. Murphy.)

you in a general way familiar with the orders affecting war housing?

A. Sale and rental of them, I was, yes, sir. [306]

Q. What was the limitation on selling as disclosed by that exhibit, if you know?

A. Well, a unit could be sold, the unit referred to as a single-family, or if it is an apartment building, a single unit could be sold for $6,000.00 or the market value, whichever is the lower.

Q. The order refers to unfurnished dwelling units. A. That's right.

Q. Is it your understanding that meant an apartment or one side of a duplex?

A. It meant that and also a single-family house.

Q. If that were involved. A. That's right.

Q. You say it was your understanding, disclosed by this, that it was $6,000.00 per unit or the market value, whichever was less?

A. That is correct, that is what it states in this.

Q. In other words, at any time while these orders were still in effect, you were permitted to sell a duplex for as high as $12,000.00 or the fair market value? A. Yes, that is correct.

Q. And you knew this? A. Yes.

Q. Yesterday Mr. Chehock asked you whether you had ever gotten tax advice concerning the sale of these units, [307] and I believe it is correct that you stated Mr. Boland had volunteered some information which he said he got from the Bureau of Internal Revenue. A. Yes, sir.

Q. Then you stated you didn't have anything

(Testimony of William K. Murphy.)

additional. A. Yes, sir.

Q. Do you have anything more to say about that today?

A. Yes, I do. As I recall it, Mr. Chehock asked me if I got any other tax advice and I think at the time I answered no or not to my recollection. At noon I had lunch with Mr. Lampe, who is our auditor, and I testified I had a conference with the Scotchman of Arthur Young & Company, I can't recall his name now——

Q. McTavish?

A. McTavish. ——and Mr. McTavish during his conference with me in the presence of Mr. Lampe, I told him I had been informed that it would be a capital gain if we sold some of our units, and Mr. McTavish stated it certainly would be. That was the extent of the tax advice.

I want to get the record straight. I didn't want you to think I was stretching it.

Mr. Chehock: Thank you. Would you mind stating when that was?

The Witness: That was the early part of May 1946.

Mr. Axelrad: Your Honor, I spoke just before we [308] adjourned for lunch of additional exhibits pertaining to the National Housing Authority regulations. Looking them over, I find that they are really repetitious, but I think the record might indicate that what we have in the record is not all of them, but what we do have, as far as I am concerned, is enough to dispose of this case on.

(Testimony of William K. Murphy.)

In other words, I don't wish to introduce any more, but I have them if anybody is interested in them.

The Court: All right. A lot of what we have already is repetitious. There may be some variations there. But you gentlemen know better than I do at this stage.

Mr. Axelrad: I am sure some of this is certainly repetitious, but it is not intentionally so.

The Court: I understand. It is part of the regulations and if it comes in there, it is in there.

Mr. Axelrad: That's all I have.

The Court: Any questions from this witness by the Respondent?

Mr. Chehock: That's all.

The Court: You are excused.

(Witness excused.)

Mr. Axelrad: Mr. Boland. [309]

Whereupon,

PHILIP PIERRE BOLAND

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your full name for the record, Mr. Boland?

The Witness: Philip Pierre Boland.

Direct Examination

Q. (By Mr. Axelrad): Mr. Boland, are you a licensed real estate broker in California?

(Testimony of Philip Pierre Boland.)

A. That's right.

Q. How long have you been one?

A. Since 1939.

Q. Have you worked actively as a real estate broker during part or most of this period?

A. Always some activity as a real estate broker except during the time, the four years I was away during the war.

Q. What years were those?

A. 1942 until 1946.

Q. You were released from the Armed Forces in 1946? A. That's right.

Q. What branch? A. Air Corps. [310]

Q. Were you an officer? A. Yes.

Q. What was your rank?

A. Lieutenant Colonel.

Q. When you were released in 1946, what did you do?

A. I took terminal leave from the time I was discharged at San Pedro, the 3rd of January, 1946, until the early part of May 1946. One of the first things I did, of course, I was just back to be discharged, and I visited different people I knew.

Among them at that time I came to visit Pool and Murphy. They showed me what they had been doing, Murphy did, and I propositioned them on the idea of selling them.

Q. Selling what?

A. The buildings that they had constructed during the war, the duplexes they had owned, that they had on hand, the rentals. They weren't interested, so

(Testimony of Philip Pierre Boland.)

I went on back to visit my relatives back in Missouri.

Q. When was that?

A. Oh, I left here in February, the latter part of January, the first of February. I wouldn't be sure what the dates were.

Q. It would be either January or February that you had been discharged and you were on terminal leave? A. That's right. [311]

Q. You approached Murphy and Pool and sought an opportunity to sell some of their property?

The Court: Let me interrupt Mr. Axelrad, it would help me with your cases if you didn't do so much summarizing as a form of question.

Mr. Axelrad: All right, sir.

The Court: I could follow your record better because I may have some difficulties there. In other words, I hear what the witness says and I will have to determine what his testimony has been, in other words. I realize that there are times when that is desirable by way of clarification.

Mr. Axelrad: That is why I did it then.

The Court: But it isn't good form as a general matter in questioning the witness.

Mr. Axelrad: Yes, your Honor. I'm sorry. In this particular case, it seemed to me he hadn't made it clear.

The Court: But you have been doing that all through this trial and it would be helpful to me if you didn't do that, Mr. Axelrad.

(Testimony of Philip Pierre Boland.)

Mr. Axelrad: I shall watch that, your Honor.

Q. (By Mr. Axelrad): Mr. Boland, when was it, exactly, that you got out of the Service?

A. The 3rd day of January, 1946. [312]

Q. And when did you first visit Murphy and Pool?

A. Shortly after that, within a week.

Q. What did you ask them?

A. Well, I was looking for something to do, looking for something to sell.

Q. And what did you suggest to them specifically, if anything?

A. Nothing in particular at that time. They had some duplexes and I said, "Well, why don't you sell them?" They weren't interested at the time.

Q. That was just casual?

A. Just casual. I wasn't even serious about it because I didn't know where I was going to land.

Q. And then where did you go or what did you do?

A. I went back to Missouri and returned here sometime in, I suppose it was in April. I talked to them again. Then I went to work——

Q. Wait a minute. You talked to them in April?

A. That's right.

Q. What did you talk about to them in April?

A. The same thing.

Q. Well, what, specifically?

A. About selling their income property, their rentals.

Q. Was this again a casual inquiry?

(Testimony of Philip Pierre Boland.)

A. Well, more or less at that time, yes. [313]

Q. Then what?

A. Then I went over to Pasadena where I learned in St. Louis, that a man I had known, who was a big operator in the real estate business in St. Louis, had moved to Pasadena, and I went over and approached him.

He said he didn't have any room for a broker, that they didn't have anything to sell.

I said, "Well, that would suit me all right, because I would like to go up and down the street and list some property. It would help me to get acquainted again and determine values."

Q. List property, you say?

A. That's right, try to get property to sell. He said that was the big job they had in mind at that time.

Mr. Chehock: With whom was this conversation?

The Witness: The broker in Pasadena whom I wanted to go to work for, Everett Davis & Sons in Pasadena.

Q. (By Mr. Axelrad): You requested permission to list property? A. That's right.

Q. What exactly is listing property?

A. Well, to go up and down the street and try to get somebody to let you list their property for sale.

Q. Were you paid for listing the property?

A. Only on a commission basis. [314]

Q. What does that mean?

(Testimony of Philip Pierre Boland.)

A. On what you would sell, if it was sold you would get a commission.

Q. If someone sold it, you would get a commission?

A. That's right. Or if I sold it.

Q. How long did you do that?

A. About 15 or 16 days.

Q. Then what did you do?

A. I made considerable money in the period of time I was there and then I found that there was nothing available for sale, that everybody wanted to buy.

Q. This had something to do with——

A. The demand was great for houses, for any kind of units, living quarters, so then is when I began to try to convince Mr. Murphy and Mr. Pool it would be a good time to sell the property.

Q. Did you have any difficulties?

A. Not with Mr. Murphy so much. He was, I would say, more or less receptive to my enthusiasm, but Pool never was very agreeable to the idea at all.

Q. Well, what did you do in the light of that disagreement?

A. I tried to convince both of them that the time was ripe for selling and they would never have as good opportunity to get rid of them again, that now was the best time to cash [315] in on them.

Q. What happened then?

A. Well, naturally Murphy saw it my way, and later on Mr. Pool more or less reluctantly agreed to go ahead and sell some of the units. It was his idea

(Testimony of Philip Pierre Boland.)

at the time that he didn't think I would be able to sell more than 15 or 20 in a year.

Q. That was Mr. Pool's idea?

A. That's right.

Q. Why not?

A. He didn't think they would sell very fast, for one thing, and he thought they were a good investment, but he didn't think people would buy income property.

Q. Why did you think that they would be sold?

A. I knew from my experience in Pasadena you could sell anything you had the right price on, and I was red hot to get hold of something good, wherever it was at.

Q. Did you try to make a deal with them to sell all the investment property?

A. Yes. I tried to get them to let me have all of it.

Q. What was the result of your negotiations with them or discussions?

A. Well, we talked back and forth and Murphy asked me to outline the whole thing, and I did. I put it down in a letter and received back a letter more or less as a receipt [316] of what I had sent, and eventually, why, they gave me the go-ahead sign, that they would sell 70 of them, the first 70 that had been built.

There was another reason, I think, that contributed to the decision on that. I had convinced them that while it was all good, the first 70 were the less desirable of their income property.

(Testimony of Philip Pierre Boland.)

Q. Why were they the least desirable?

A. They were built at a time when the bath tubs were more or less home-made, and over a long period they might not be as good an investment as the others. They were not quite as good buildings as the latter 100.

Q. Were you able to convince them on the 70?

A. Yes.

Q. What was the arrangement you made with them concerning the 70 duplexes?

A. Well, they said, "What do you want for selling them?" .

I said, "I want the straight five per cent commission for selling them, like any other broker gets."

Q. What do you mean? Was that something fixed by law?

A. No. It is more or less traditional out here. If you don't establish it any other way, you get five per cent. That is what the Real Estate Commission will back you up in.

Q. Five per cent of the sales price? [317]

A. That's right.

Q. What was the result of the deliberations or negotiations?

A. Then we got into a discussion. Mr. Pool thought if we were going to sell them, they ought to be painted, and that would have delayed the time and would add something to the price. So I finally talked him out of that.

Then we arrived at a figure that they would give me $500.00 a house, and inasmuch as there were not

(Testimony of Philip Pierre Boland.)

any offices available there, that I didn't have an office, that it was difficult to get a telephone and different things, that I could use their office and use whatever facilities were available and they would give me $500.00 per building in lieu of the straight five per cent commission.

Q. Was that arrangement actually put into force? A. That's right.

The Court: $500.00 per building?

The Witness: That's right.

The Court: How many buildings are there?

The Witness: There were 70 buildings.

The Court: 70 buildings and they were duplexes?

The Witness: That's right.

The Court: In other words, the living units were twice 70?

The Witness: That's right. [318]

Q. (By Mr. Axelrad): You actually did carry out between you what you had agreed to do, you said? A. That's right.

Q. What were you to do? What were your duties in selling these?

A. General duties of a real estate broker.

Q. What are they?

A. Well, for me it was merely a question of taking over the entire deal and selling it as I chose, as long as they told me what they wanted for the building and what I was to get. I would use whatever method I presumed was satisfactory to sell those buildings.

Q. What methods did you use?

(Testimony of Philip Pierre Boland.)

A. General ones, advertising and having the people come in, and selling them.

Q. Did you prepare the advertising?

A. I wrote all the ads, yes.

Q. I show you—well, I don't find it here.

A. What are you looking for?

Q. An advertisement of Artcraft.

Mr. Chehock: Which one do you want? Here it is right here.

Q. (By Mr. Axelrad): I hand you Respondent's Exhibit BBB and ask if this [319] is representative of the ads or advertisements that were prepared in relation to the 70 duplexes? This appears in the paper of May 4, 1946.

A. That's right.

Q. Did you prepare that? A. I did.

Q. Did you prepare all the advertisements?

A. All of them, yes.

Q. What papers were they in?

A. The Herald Express, the Los Angeles Examiner, the Los Angeles Times, and occasionally in the Long Beach Press-Telegram.

Q. This advertisement is signed, or it is printed at the bottom, "Artcraft Builders, Inc., 2187 Longwood Boulevard, Long Beach."

A. Lakewood Boulevard, that is.

Q. Oh, yes, Lakewood Boulevard, Long Beach. What was the purpose of putting in an advertisement like that if your testimony is correct that you were selling this property for Mr. Murphy and Mr. Pool?

(Testimony of Philip Pierre Boland.)

The Court: I don't know whether he has been too definite about that.

Mr. Axelrad: Let me withdraw that question and back up. [320]

Q. (By Mr. Axelrad): Who did you make your arrangement with to sell the property, who were you dealing with?

A. Mr. Pool and Mr. Murphy.

Q. Were you dealing with Artcraft Builders, Inc.?

A. Yes. They were representing Artcraft, as far as I know. They were Artcraft Builders.

Q. Who was Artcraft Builders?

A. Mr. Pool and Mr. Murphy.

Q. You mean they were officers of Artcraft?

A. That's right.

Q. Who owned this property you were selling, if you know? A. Pool and Murphy.

Q. Were you selling it for the owners?

A. That's right.

Q. And how did Artcraft's name get into the advertisement?

A. Well, it was a matter of orientation. The property was known as the Artcraft Manor, and these mats, the signature mats, the newspapers had them, and it was a question of utilizing to the best advantage any tool that was available to sell the property.

Q. Did you consider that there was anything dishonest about saying Artcraft was selling something when you knew it wasn't? [321]

(Testimony of Philip Pierre Boland.)

A. No, not at all.

Q. Why not?

A. It was merely a matter of advertising. There was nothing unusual about it. It is like you eat or feel or sleep better if you smoke Philip Morris cigarettes. Those things are traditional in the real estate field. One of the Deputy Real Estate Commissioners asked me about it and he was satisfied.

The Court: What do you mean, a Deputy Real Estate Commissioner asked you about it?

The Witness: We have pretty close supervision of the brokers and how they sell property by the Real Estate Commission of California. One of them came and asked me, and talked to me about it, and didn't object.

The Court: You mean at the time these ads were being run?

The Witness: That's right.

Q. (By Mr. Axelrad): Do you know how the Real Estate Commissioners would have taken notice of something like that? They didn't know who was selling these, did they?

A. They do. They keep track of these things. Some real estate brokers might have squawked. I don't know. He came and asked me about it. [322]

Q. Did you ever discuss with Mr. Murphy or Mr. Pool the way in which you were going to advertise these?

A. I reserve the right when I make a deal to sell the way I want or——

(Testimony of Philip Pierre Boland.)

Q. You are positive you prepared the advertisements in all cases? A. Absolutely.

Q. Regardless of what paper the ad appeared in? A. That's right.

Q. And did you have anyone employed by you in this selling operation?

A. I had two salesmen, and at one time I had a girl in the office that took care of the work for me, in addition to the help that was given by the lady that worked for Artcraft.

Q. Did Mr. Murphy and Mr. Pool give you any assistance?

A. No, no assistance. Mr. Murphy several times made suggestions that didn't have any value to them. I didn't pay any attention to them. Mr. Pool never even spoke to me about the thing while I was selling them.

Q. Were they around the office a great deal of the time?

A. No. They were there sometimes. Mr. Pool came by a few times. He was doing, as I remember, more than anything else, pistol shooting and I took time out once in a while [323] to look at his collection of pistols.

Mr. Murphy was out and in. They weren't there too much. Occasionally they would drop in.

Q. And you prepared escrow instructions or dictated the escrow instructions on behalf of the seller?

A. I did.

Q. How did that occur, where did it take place?

A. Well, it was sort of a mass production plan

(Testimony of Philip Pierre Boland.)

after I got it rolling with the Bank of America. It was set up and they knew exactly what we wanted from each one of these and how they were set up.

Q. Did you take the buyer down to the bank and do it down there?

A. Not always took the buyer down there.

Q. Or meet the buyer.

A. The thing sort of snowballed a little faster than I anticipated, so at times I would have more people waiting to buy and I wouldn't even get to take the orders and escrows down the same day. Sometimes I would take a bunch of them down to the bank, and there was a woman who was set aside especially by the bank to take care of them, and she would call the people to come in to sign the escrows.

Q. How long did it take to sell all these 70, now? A. I would say ten weeks, probably.

Q. How much were you paid for selling the 70?

A. $500.00 a building.

Q. That would be $35,000.00?

A. That's right.

Q. Do you know what your expenses were?

A. Well, they ran about—the advertising wasn't too expensive. I would say it was around $2,500.00 in round figures for the 70. The rest of it was the expense of hiring a girl. I had no brokers or salesmen helping me sell the 70. I did it all personally.

Q. What about credit reports?

A. I made the buyer pay for them.

Q. You made the buyer pay for that?

(Testimony of Philip Pierre Boland.)

A. Yes.

Q. You added that onto the cost?

A. Yes.

Q. Did you do the work of securing the name and all of that data?

A. No. I made a deal with the bank that they would let me use the slips whereby they requested credit. In other words, I saved a couple of bucks to the buyer. The Bank of America had a rate of $2.50, as I recall it, on each credit report. By using that method and requesting it there, they would get a report a little faster, and it was a little cheaper.

Q. After the 70 were all sold, what happened?

A. I went on a vacation. I went back to Missouri and got married.

Q. Then what?

A. I took a little time off, came back, and continued to proposition Murphy and Pool on selling the rest of them.

Q. The 100? A. The 100.

Q. What about the 22?

A. I never got very far with those, because they were evidently a prize possession and they didn't want to sell them.

Q. Did you ask them to sell?

A. Yes. I wanted to sell everything they had while I was there. I wanted to sell the market they had, too.

Q. When you got back from the wedding trip you refer to, when was that?

A. About the middle of July, the 10th of July,

(Testimony of Philip Pierre Boland.)

I think it was. I was married on the 6th of July and came back right afterwards.

Q. Then you went back and contacted Murphy and Pool? A. Yes.

Q. With what result?

A. They still didn't want to sell.

Q. Tell us what led up to the final agreement to sell.

A. I convinced them, at least I thought I convinced [326] them the others sold so fast, and if they were ever going to make a quick recovery on their investment, it was the time to do it, before everybody else got in the field, and I thought, I didn't know, I thought we were approaching a point where we could sell them with no down payment, which had never been done.

Q. How do you mean that you could sell with no down payment?

A. By selling to veterans on G.I. loans. That is what we were eventually to accomplish. I believe it was the first time in California anything like that was ever sold with no down payments.

Q. In your experience as a real estate broker, do you find it easier——

The Court: What do you mean by no down payment? They got a veteran's loan, didn't they?

The Witness: If two veterans would go together, the G.I. loan was sufficient, they didn't have to have a down payment other than the impounds for expenses. The lending agencies would loan it all. Each had $4,000.00, which made $8,000.00, plus the rest

(Testimony of Philip Pierre Boland.)

of the money they would get from the Building and Loan.

The Court: By that you mean they didn't have to pay anything over and above what they borrowed?

The Witness: That's right. They borrowed the full [327] amount.

The Court: As far as the seller is concerned, it was cash, wasn't it?

The Witness: That's right.

Q. (By Mr. Axelrad): Were Mr. Pool and Mr. Murphy willing, if necessary, to accept any notes or trust deeds back if you couldn't get all cash, or didn't that question come up?

A. It never arose that I know of.

Q. When they gave you authority to sell, did they give you authority to sell under any terms or any price, or was it fixed?

A. The price was fixed.

Q. Not the terms, nothing was said about that?

A. Nothing was said about that, about getting cash. They got the cash whenever they got the lending agencies, which we did, the banks, to take it, why, it was cash to them.

Q. Did you have anything to do with arranging the financing on these hundred?

A. Yes, I helped.

Q. Was there any problem that arose concerning it? A. Not at all on the first 70.

Q. I am talking about the hundred.

A. Oh, the 100. We ran into a little trouble.

(Testimony of Philip Pierre Boland.)

The Bank of America wanted these loans and they actually solicited [328] me to bring them there, the manager of the Bank of America, the first 70, and they were all sold, almost without exception, I think in every case, to one individual buyer.

But the 100, when we instituted the idea of two veterans buying with no down payment, and I ran the ads and sort of got ahead of myself and picked up some sales real quick, and then the Bank of America wouldn't go for it.

They said, "We don't want to loan unless it is one purchaser only. We won't take two."

The Court: You said the 70 were all sold to one purchaser?

The Witness: Yes.

The Court: You mean one purchaser would buy a duplex?

The Witness: That's right. In the later 100 cases, 100 houses, duplexes, almost without exception, all of them were sold to two buyers together.

Q. (By Mr. Axelrad): They took them as joint tenants? A. That's right.

Q. You didn't try to deed it separately down the middle? A. No.

Q. And the bank wouldn't——

A. They took it back, the money. [329]

Q. Did they say why?

A. They said they didn't want that kind of loan.

Q. What happened, what did that do to your plans?

A. We were stalled for a week or two and we

(Testimony of Philip Pierre Boland.)

made another move then and had Mr. Murphy talk to, I believe it was the Western Federal here, who was the original lender on some of these buildings. Pretty soon they didn't want them.

So we finally ended up by taking them to the Insurance Funds Mortgage Company and they bought all of them that the Western Federal had already taken from us, plus the additional ones I sold.

Q. This was the Massachusetts Insurance Company?

A. I think that is where they got the money.

Q. Did that delay the process on escrow?

A. Yes.

Q. In what way?

A. Well, these that had been taken to the bank, they didn't want them, so they were held up there, and the Bank of America was willing, wanted to go ahead and do the escrow on all of them, on the 100, the same as the 70, but they didn't want to make any loans on them.

Q. One of the exhibits in this case indicates that in the August sales there was a delay between the opening of the escrow and the placing of the grant deed in escrow. [330]

A. Yes.

Q. Do you know why that occurred?

A. I can't put my finger on anything I would say would be solely responsible for it. There are a number of things that could contribute to it. We had to have new deeds printed.

(Testimony of Philip Pierre Boland.)

Q. Why?

A. Well, it was a different tract number and it was a different setup on the sale, and part of that I think was due to the fact that when I put these 100 duplexes on the market, I was never so worn out in my life trying to sell something. Half of them I did sell would cancel in a day or two, change their mind, come back and want their money back, and when I would go out to eat at 6:00 o'clock in the afternoon, I would come back and there would be 40 or 50 people there and I wouldn't have time to go to the bank.

I finally had to have a couple of salesmen, people to help me. When you advertise no down payment, the people just flocked in.

Q. And I suppose the people with no down payment would come in then?

A. Yes, and they would put up their impounds, and the next day they would come in and say they wanted it back. There was some delay in making arrangements for a new loan in the beginning.

Q. Were you instructed by either Murphy or Pool or anybody authorized to act for them, to delay putting the deeds in escrow? A. Never.

Q. Was there any discussion about whether there was a sufficient holding period?

A. It was never mentioned to me.

Q. Was anything about the tax results of these sales mentioned at any time in your negotiations or sales on their behalf?

A. Somebody raised the question of long term

(Testimony of Philip Pierre Boland.)

capital gains, and I wasn't familiar even with what they meant. My interest was in selling. However, I did come up here——

Q. What do you mean, "up here"?

A. Up to Los Angeles, the Revenue Department, and tried to get some information on what long term capital gains were, to what that applied, and various information as regards the taxes.

Q. What information did you get?

A. I didn't get anything except they referred me to various decisions and rules and regulations.

Q. Did you relay what you found out to Mr. Murphy?

A. In my own judgment, I figured they were in the clear if they wanted to take capital gains. However, I never did discuss it with them. I just [332] mentioned to Murphy I thought it was all right.

Q. This was your advice? A. Yes.

Q. And not the Bureau's advice? A. No.

Q. It was your interest to sell them, to do this?

A. Yes.

Q. Were you acting objectively as a real estate broker? A. That's right.

Q. Did you have any other qualification to give that advice?

A. Well, from the long range, in my early days, I practiced law, and at one time worked in the Revenue Department, so from a long time ago I was familiar with what they would try to tell me about taxes.

Q. On these 100 houses, when you were so busy,

(Testimony of Philip Pierre Boland.)

with 40 or 50 people there at a time, did you ever get any help from Murphy or Pool? A. No.

Q. Did you ever get any help from their office force?

A. Yes. Miss Woodruff, who was working for them, for Artcraft, was familiar with the office and gave me a great deal of help.

Q. By help, do you mean advice?

A. Sometimes she would pitch in and do a little work for me. [333]

Q. Fill out documents?

A. That's right, take credit reports, information.

Q. Was this part of your arrangement with Mr. Murphy?

A. Yes. That was all right, that was satisfactory.

Q. Was that spoken about in advance?

A. Yes.

Q. What else do you recall from the people in the office? Some secretarial help?

A. Yes, and use of the telephone. I couldn't get one.

Q. You couldn't get a telephone?

A. I tried to get one and you couldn't get one at that time.

Q. Why not?

A. You had to wait. The trunk lines weren't available. It is almost as bad now, for that matter.

Q. I believe I asked you earlier, and then we got off to something else without an answer, but in your experience as a real estate broker, which is

(Testimony of Philip Pierre Boland.)

in selling in this area that we are talking about, is it easier to sell a duplex or a single-family unit?

A. It is always easier to sell a single-family.

Q. Why?

A. Less money is needed and there are more people with a sufficient amount of money to pay [334] the down payment. In addition, where you have the climate, most people would like to have a home where there is an individual yard. It is easier to sell. I am building homes now. I wouldn't think of building anything but small individual homes.

Q. These advertisements, were you present when Mr. Chehock read from them about how they would pay for themselves, some of them said?

A. Yes, I was here.

Q. What was the purpose of such advertising?

A. It is to sell the property.

Q. Did you think of these sales schemes or were they generally used?

A. They are generally used. But when you advertise that a duplex, or a piece of income property, that part of it will carry the other one, you don't necessarily limit the consideration to the particular month or year. You figure over a basis of 12 or 15 years to carry it. If one unit won't carry the other one, it is not properly built or not properly located.

Q. How long did it take you to sell these 100 duplexes?

A. Well, the first, they went fast, and then along

(Testimony of Philip Pierre Boland.)

toward the last they slacked off because other people started to do the same thing and sell at no down payment.

Q. Were you the first one to sell without a down payment? A. Yes. [335]

Q. How do you know that?

A. That is what the newspapers told me, the first ad of that kind to go in. I had to fight to get it in the papers. They objected to running ads that were different, that are new and offer more. I had no trouble with the Examiner and the Herald, but I had trouble with the Los Angeles Times. I had to go up and fight to get it in there.

Q. Because they thought it was untruthful?

A. That's right.

Q. After you finished selling the 100 duplexes, then, as far as Mr. Murphy and Mr. Pool were concerned, did you ask to sell anything else?

A. I wanted to sell the remaining property they had there. They had some vacant property which I wanted to sell, but they eventually built a market on it, rather, a bank. I also wanted to sell these other buildings they had, but they were not in the mood.

Q. The 22 apartments? A. Yes.

Q. Did you make a determined effort to get them to sell that?

A. Not so determined as the other, because there were better reasons for them to keep them.

Q. The 22? [336]

A. Yes. They would be harder for me to sell.

(Testimony of Philip Pierre Boland.)

They were four units. It takes more money. The people couldn't buy it like they could the others sold.

Q. Would it be a correct statement that the more units there are, the more difficult the sales might be, the number of units in a building, I mean?

A. You mean if there were 200 units in one building?

Q. You were talking about the apartments having three or four units. A. Yes.

Q. Would that make it more difficult to sell than a duplex, say?

A. Well, in some instances, it might.

Q. It is difficult to generalize about that?

A. That's right. It depends on your location and your neighborhood.

Mr. Axelrad: I wonder if it would be possible to have a very short recess. I have an emergency long distance call on a family matter. It is very important.

The Court: All right. We will take the intermission.

(Short recess taken.)

Mr. Axelrad: I have completed my examination of Mr. Boland.

Mr. Chehock: Your Honor, before I start cross [337] examination of Mr. Boland, I would like to read information that I just received over the phone. I also had a call waiting for me from the Federal Housing Administration here in town.

The Court: All right.

(Testimony of Philip Pierre Boland.)

Mr. Chehock: I will quote a telegram that was received here in Los Angeles from Washington, D. C., which reads as follows. This telegram was sent from Washington, D. C., on October 15, 1945, addressed to John E. McGovern, District Director, Federal Housing, here at Los Angeles, and is signed by Raymond M. Foley, Commissioner, FHA. This is the telegram.

"Revocation of L 41 effective October 15 results in removal of sale ceilings on all priority assisted housing and eliminates all other priority operations formerly performed by this agency. OPA controls over rental remain."

It is signed Raymond M. Foley, Commissioner of FHA.

Petitioners' counsel states he is willing to stipulate that this is a correct statement of this telegram.

The Court: Very well.

Mr. Chehock: Is that correct?

Mr. Axelrad: Yes.

The Court: The record will show that. [338]

Cross Examination

Q. (By Mr. Chehock): Mr. Boland, could you describe a little more in detail this office that you operated out of in selling the 70 and 100 duplexes, how many rooms it has and just describe it generally? A. Just one room.

Q. Just one room? A. Yes.

Q. What were the dimensions, approximately?

(Testimony of Philip Pierre Boland.)

A. I would say about a third the size of this room.

Q. That doesn't mean much in the record. Could you give me some approximate measurement?

A. It was not a square. It was not a rectangular room. It was on the curve of the building. It was probably 25 feet across one way and 20 another. Across the back, it was a little farther. Then the bathroom was to the rear down back of a store. It was a corner of a market building that was taken off.

Q. You said the dimensions were approximately what?

A. Well, I can explain it better this way. I would say it was perhaps 400 square feet that were in the place.

Q. Who was working there?

A. Mrs. Woodruff and a girl that worked for me and myself. [339]

Q. It was also the headquarters of Arteraft Builders, Inc., wasn't it? A. That's right.

Q. And of Edward Pool and Associates?

A. That's right, so far as I know.

Q. This Ruby Woodruff worked for Arteraft and for Edward Pool and Associates? A. Yes.

Q. And she assisted you?

A. To some extent.

Q. Were there ads around the building there indicating that the 70 and the 100 were for sale, some signs? A. Not in the office, no.

Q. Was there on the tracts? A. No.

(Testimony of Philip Pierre Boland.)

Q. There were no printed signs up anywhere, painted signs?

A. I had a couple of my own signs up the first week or so in front of the buildings, the two buildings that had vacancies in them, but I took those down. The people would come to the office and I would send them up to the places that were vacant. I said, "If you want it, come back and we will do business here." That had to do with the 70, all of them, the 70 and the 100. They were sold identically the same way. [340]

The Court: You had some vacant in each place?

The Witness: That's right. Whenever I could get one vacant, I would send them to that one.

Q. (By Mr. Chehock): Did the building that you operated from have some sign there indicating that it was the offices of Artcraft Builders, Inc.?

A. A sign across the front and on the windows.

Q. What did it have?

A. Artcraft Builders, Inc.

Q. Did it have any other signs indicating who was officing there?

A. Not that I know of. I believe there was a sign in small letters on the window of an engineer by the name of Martin, who at one time had done some work, I presume. I think I have been told that, that had done some work for either Mr. Pool or Mr. Murphy, and had a small sign on the window for a while.

Q. Were there any signs on the windows or anywhere else on the building showing your name?

(Testimony of Philip Pierre Boland.)

A. No.

Q. Did you have a written contract with Edward Pool and Associates or the Murphys and Pools? A. No.

Q. With regard to the sale of the 70 and 100?

A. No.

Q. You had an exchange of letters?

A. An exchange of letters.

Q. Do you have those letters? A. No.

Q. Did you look for the letters? A. No.

Q. You haven't looked for the letters?

A. No. I don't keep anything. When I finish a job, the record is finished as far as I am concerned.

Q. Do you have those letters?

A. I don't think so. If I have, they are buried some place, and I don't know where they are at.

Q. Do you know when they were written?

A. I wrote a letter and it was answered sometime during the time I was working this short period in Pasadena.

Q. That would be when?

A. Well, April 1946.

Q. Did the letters cover the 70 and the 100 duplexes?

A. My letter covered the details and the possibilities of what could be done, and Murphy's letter to me sort of made a recap of the whole thing, that this would be the way it would be if we would sell them, if they were to be sold.

When we finally made the agreement, Mr. Pool

(Testimony of Philip Pierre Boland.)

said, "All right. It is $500.00 a building. Go ahead [342] and see how many you can sell. Sell them as fast as you can get them empty, or if you can sell them to the people in them, all right."

You wouldn't have to worry too much about commission, you see. When you start in to sell a piece of property out here, you know you are going to get your commission, so a written contract doesn't enter into it. It never does with me.

Q. Isn't it true under Section 1624, I think it is, of the Civil Code of California, a real estate agent might have difficulty collecting his commission unless he had it in writing?

A. A real estate salesman might. A broker wouldn't. I don't know what you are referring to.

Q. The Statute of Frauds.

A. I never have known anybody to have any trouble collecting a commission.

Q. Do I understand from your testimony that this correspondence that you are mentioning back in—did you say April of 1946?

A. I think it was around there.

Q. Had reference to the 70 and the 100 duplexes?

A. I wanted to sell them all, yes.

Q. In dealing with these various prospective buyers and in advertising the property, and so [343] forth, did you put yourself out as acting for and on behalf of Artcraft Builders, Inc. in selling these?

A. No.

(Testimony of Philip Pierre Boland.)

Q. Did you sign letters going out under the name of Artcraft Builders, Inc.?

A. It is possible I might have. I don't remember doing so. I had my own stationery. I wrote them as a real estate broker.

If it had something to with perhaps the lease or something that had to do with Artcraft itself, the letter might have gone out as something from Artcraft.

Q. I hand you this letter, Mr. Boland, and ask you if that is your signature?

A. That is my writing.

Mr. Chehock: Counsel would like to have me state that there are not others found of that type in these files. The facts are that all we have in these files are copies of letters and this appears to be an original.

Q. (By Mr. Chehock): Did you write a number of letters of that type under the name of Artcraft Builders, Inc.?

A. I doubt it very much. I might have had this letter written as going out—after all, this has nothing to do with the selling of them. I beg your pardon. It has. As a rule, these people were told about this by telephone or in person. I might have written other letters. I don't know. [344]

That is my writing on that.

Mr. Chehock: I am willing to state for counsel's satisfaction, in going over these files I didn't find other letters of this type, but I didn't find any of the originals. All of them are copies of letters, but

(Testimony of Philip Pierre Boland.)

I did find this original and I would like to introduce it.

The Court: Are you offering it?

Mr. Chehock: I am offering it.

The Court: Any objection?

Mr. Axelrad: No objection, except I would like to note in this connection that there is no indication this ever went out of the office, since they still have the original.

The Court: Let's see it.

Mr. Axelrad: For all that appears, it may have been just a mistake.

The Court: It may be received and marked as Respondent's exhibit next in order.

The Clerk: Respondent's Exhibit GGG.

(The document above referred to was received in evidence and marked Respondent's Exhibit GGG.)

Mr. Chehock: I am offering that in evidence, your Honor.

The Court: It has been admitted. [345]

Q. (By Mr. Chehock): I hand you Exhibit VV, on which you will note that there are some letters going out there, copies of letters, rather, apparently to the tenants, advising them of the new owner. A. Yes.

Q. These are merely copies and they are written under the name of Artcraft Builders, Inc., "By," and it is blank, and over at the left-hand side is R. W. A. Yes.

Q. Were those sent out by you? A. No.

(Testimony of Philip Pierre Boland.)

Q. By whom were they sent out?

A. I presume by Artcraft, Ruby Woodruff, secretary.

Q. Did you handle this end of it? A. No.

Q. Were these sent out as a part of the course of your work?

A. When the deal is finished and it is signed in escrow, that is when they should go out from the owners.

Q. Are these files here, of which Exhibit VV and WW are a part, your files?

A. Well, this part here would be mine.

The Court: That is the top one?

The Witness: That is the top one. This has to do with the sale. [346]

Q. (By Mr. Chehock): If you don't mind, will you be just a little more specific or explicit on what you are talking about when you say "this"?

A. That is this order here, where you take an order to sell a piece of property, and this is——

Q. By "this," what do you call it, a contract?

A. That's right.

Q. Of May 5, 1946, in Exhibit VV.

A. Yes.

Q. What do you say about that?

A. This is the part that has to do with making the sale. This is the part that the broker is interested in.

Q. All right.

A. Outside of getting the deed to go through escrow and the escrow instructions, that is the end

(Testimony of Philip Pierre Boland.)

of it as far as the broker is concerned. This has to do with——

The Court: What are you talking about now?

The Witness: This letter that has to do with telling them where to pay their rent or handle the transactions, had no part of my work whatsoever, and I was not interested. Why they are put together, I don't know.

Q. (By Mr. Chehock): Is this your copy of the escrow instructions? [347]

A. I wouldn't know.

Q. Are all of these files there in those two boxes your files, your copies of files?

A. I don't know. I haven't looked at them.

Q. Do you want to step down and look at them?

A. I couldn't tell by looking at the boxes. They probably are.

Q. I want you to testify. If you have any doubt, you can go over and look at them and see.

A. What I mean is, after six or seven years time, I can't look at a piece of paper and tell you.

The Court: Go down and take a look at them.

(Witness leaving stand and going to exhibits.)

The Witness: They are all my envelopes there, and this is my writing, your Honor.

Q. (By Mr. Chehock): By "this" you are talking about—— A. This right here.

Q. All these are your files.

A. I don't know what all this is. What has been

(Testimony of Philip Pierre Boland.)

put here afterwards, I can't tell. I don't know what has been done. I left them when I left the job.

Q. Just come over here, please. The pack you are looking at is of the same type as Exhibit VV, is that not true? [348]

A. I don't know, unless I go through them.

The Court: Well, take a look at them. You can tell. You know enough about these things not to be so vague as that. Now are you able to state?

The Witness: I presume they are, yes.

The Court: They appear to be to you?

The Witness: That's right, they appear to be, yes.

The Court: All right.

(Witness resuming stand.)

Q. (By Mr. Chehock): I refer you to Exhibit WW and below the place of signature on the escrow instructions where the signature would be for William K. Murphy, Edna M. Murphy, Edward Pool and Lottie Pool, "By," appears in typing, "Signing date 9-23-46." Can you explain that, why that is on there and when it was put there?

A. No, I can't definitely explain it. I presume it is when this copy was made that the signing date—this is taken from the other one. A copy was made from the original and the other was signed 9-23-46.

Q. What do you mean by "the other one"?

A. It must have been the original of this copy.

(Testimony of Philip Pierre Boland.)

They don't always sign the copy. They would sign the original.

Q. Did you have that typed on there?

A. I don't remember. [349]

Q. Who would have it typed on there?

A. The bank that handles it, as a rule, might have. The bank that handles the escrow. Some of these escrows were mass production and they could have signed some of these in advance. The escrow instructions were similar for all these buildings. They would do, maybe, the same as they sign all the deeds at one time.

Q. I am referring to Exhibit O-15, Lot 1. That was placed in escrow on October 14, 1946, bearing a date of September 23, 1946.

The Court: What was bearing the date of October 14th?

Mr. Chehock: A grant deed.

The Court: The deed?

Mr. Chehock: Yes.

Q. (By Mr. Chehock): Now, I refer you to the escrow instructions for that lot number and ask you to state what is typed under the line for the signature of the Murphys and Pools.

A. The signing date, 9-21-46.

Q. While we are talking about Lot 1, I find also in your files here for these 100 duplexes that there is a card, which I hand to you and ask you if you can explain what that is.

A. Yes. This is a simple memorandum so that I [350] wouldn't sell the same building to two peo-

(Testimony of Philip Pierre Boland.)

ple. It has the number of the place, and when it was sold, I take this out of the box.

Q. What is this here, "No Lease" opposite both places?

A. That is not my writing. I presume it is Mrs. Woodruff's writing, and it meant at the time I made this up there was no lease on either of these apartment units.

The Court: That is a card from files you kept?

The Witness: That is a card from files I kept in a little box, because I had the misfortune to sell one place to two people and from then on whenever I did sell I would take it out completely and put it with this envelope.

The Court: All right.

Mr. Chehock: The Respondent offers in evidence the card the witness has just referred to.

The Court: Any objection?

Mr. Axelrad: No objection.

The Court: It may be received and marked the next exhibit number.

The Clerk: Respondent's Exhibit HHH.

(The document above referred to was marked Respondent's Exhibit HHH and was received in evidence.)

Q. (By Mr. Chehock): I hand you these files for Lot 2 in Tract 13163, and ask you to state what [351] your card shows in regard to the leases of the two units in that duplex at the time of sale.

A. This one has written there "No lease."

Q. For both of them? A. That's right.

(Testimony of Philip Pierre Boland.)

Q. Is there any date appearing under the place for the signature of the Murphys and Pools as to the signing date? A. Not on this copy.

Q. Not on that copy. Now I refer you to your files for Lot 3 and ask you to state in the record what your card indicates as to whether or not there is a lease on either of these units in that duplex.

A. "No lease," it says on there.

Q. No lease for both units?

A. That's right.

Mr. Axelrad: Your Honor, I would like to interpose an objection at this point. The witness has testified that that writing with respect to whether there is a lease or not was not there, and I think the implication is going into the record, when Mr. Chehock has him read it, that he is testifying he wrote it and there was no such testimony.

The Court: If you will take a look at them, then you would know. If you want to take a look, come on around and look at them.

Mr. Axelrad: We have stipulated with respect to all the leases. I don't know what this is all about. [352]

The Court: You stipulated some things about the leases.

Mr. Chehock: We stipulated there weren't any more leases made after a certain date in April, but I am putting into the record places on which there were no leases at the time of sale.

Mr. Axelrad: Are you going to put into the record where there were leases?

(Testimony of Philip Pierre Boland.)

Mr. Chehock: I intend to put into the record—I would like to have stipulated all that, but you didn't want to, and consequently I am going to put in through the Revenue agent a summary of all these cards, but it will take too long to go through every one of them.

The Court: All right.

Mr. Chehock: I am doing this as merely laying the ground work.

Mr. Axelrad: I suggest he is laying it with the wrong witness, since he says this is not his writing.

The Court: Well, wait a minute. I don't think we need to go on at all. These are this man's cards?

Mr. Axelrad: That's right.

The Court: They are the cards he has been asked about and he hasn't expressed any doubt about them. The first one did have some pencil writing on it. That is something else again. As of now, [353] I see no basis for sustaining the objection. The objection is overruled.

Mr. Axelrad: Exception, your Honor.

The Court: Exception noted.

Q. (By Mr. Chehock): Will you state also in the record how the words "No lease" are written on this particular card for Lot 3? A. Printed.

Q. In ink? A. That's right.

The Court: It is on there in the same style of writing or printing as the word that goes before it?

The Witness: No. This is different. The other one was lined.

The Court: I am talking about this card.

(Testimony of Philip Pierre Boland.)

The Witness: Yes.

The Court: All right. In other words, it is printed in ink.

The Witness: Yes.

Q. (By Mr. Chehock): Will you state under the escrow instructions whether or not there is any designation there as to the signing date?

A. No.

Q. We have previously referred to Exhibit WW, which covers Lot 4, and which you have testified, have you not, has typing there below where the [354] signatures of the Murphys and Pools are, of "Signing date 9-23-46," is that right?

A. That's right.

Q. Now I refer you to your files for Lot 5 of Tract 13163, and ask you to testify as to what the card there indicates in regard to leases.

A. It says, "No lease" on both units.

Q. How is it? A. Typed.

Q. The words "No lease" are typed?

A. That's right.

Q. Will you further testify whether or not the place below where the signatures of Murphys and Pools on the escrow, whether or not it states the signing date? A. Nothing there.

Q. I hand you your files for Lot 6 in Tract 13163, and the card, and ask you to state what the card indicates as to whether or not the property was leased at the time of the sale.

A. It apparently was for one unit and not for the other one, according to this card. It says "No

(Testimony of Philip Pierre Boland.)

lease" on one and the other says "Lease, W. O."

Q. What does that mean?

A. I don't know.

Q. I hand you the escrow instructions and ask you whether there is any signing date typed in [355] there where Murphys and Pools signatures would appear. A. No.

Q. I hand you now your file for Lot 7 in Tract 13163, and ask you to state what the card there indicates as to whether or not either of the units in the duplex was leased.

A. Apparently one of them was leased.

Q. Will you state just what the card says?

A. The card says "No lease" on 2226, and it doesn't say anything except the date after, 11-13-46.

Q. After which property? A. 2224.

Q. 2224 Grand Avenue? A. Yes.

Q. That would indicate that the lease on the unit for 2224 Grand Avenue would expire November 13, 1946, is that right? A. I think so.

Q. I ask you if there is anything below the place where the signatures of the Murphys and Pools on the escrow instructions appear signifying when the signing date is to be. A. Nothing.

The Court: Let me inquire. You have a number of those. Do you propose to go through each of those and ask him what appears on those cards? Is that the idea?

Mr. Chehock: There are a hundred of them and I am taking as a fair criterion the first ten.

The Court: What I am asking is what you plan

(Testimony of Philip Pierre Boland.)

to do with the remainder. What you have done with these is ask him about them.

Mr. Chehock: Yes.

The Court: Now you show him the card and ask him what is on there.

Mr. Chehock: Yes.

The Court: I don't see why we need to do that, [357] if it is just by way of a sample. If you are going to have an abstract made of these things, they can be checked against the record and you wouldn't have to have all this testimony on them.

Mr. Chehock: I would like to have the record show for the various deeds, they were placed in escrow in August——

The Court: Is that all you are going to do now?

Mr. Chehock: Yes.

The Court: Is this August?

Mr. Chehock: No. I am giving August as well as the others, to show that in the others they do not have a signing date. On the August the escrow instructions specify as to what the signing date is to be.

The Court: I see.

Mr. Chehock: I want the record to show what that is.

The Court: Well, you better show all of your August ones, then.

Mr. Chehock: I was first showing the first ten, to show both kinds, to show the difference, and then I was going to show the August next.

The Court: All right.

(Testimony of Philip Pierre Boland.)

Q. (By Mr. Chehock): I refer you to your file for Lot 8 and ask you what your cards indicate [358] as to whether or not these units were rented at the time of sale.

A. 2228 Grand Avenue, no lease. 2230, apparently leased to 11-9-46.

Q. Will you state under the escrow instructions where the signatures of Murphy and Pool would appear, what appears there?

A. The signing date, 9-23-46.

Q. I hand you now your file for Lot 9, Tract 13163, and ask you what the card indicates with regard to the lease situation at the time of sale.

A. No lease on both of them.

Q. I hand you the escrow instructions and ask you whether there is anything below the place for the signature of the Murphys and Pools as to the signing date. A. Nothing.

Mr. Axelrad: May I see one of those to see what you are trying to get at?

Mr. Chehock: Certainly.

Q. (By Mr. Chehock): I hand you your files for Lot 10 in Tract 13163 and ask you to state what your cards indicate with regard to the leases on these units at the time of sale.

A. No lease on either unit.

Q. How is it placed on the card?

A. One in ink and one typed. [359]

Q. Now I refer you to the escrow instructions and ask you if there is anything there signifying the date for signing for the Murphys and Pools.

(Testimony of Philip Pierre Boland.)

A. Nothing.

Mr. Axelrad: May I see that? I would like to see where you are reading from.

Mr. Chehock: Right there (indicating).

The Court: Down at the bottom of the escrow instructions.

The Witness: Could I see the card a minute?

Mr. Chehock: Yes.

Mr. Axelrad: Where does it say "signing date," or should say it?

Mr. Chehock: It doesn't on this one.

Mr. Axelrad: Do some of them say "signing date"?

Mr. Chehock: Yes.

Q. (By Mr. Chehock): Now, if we go down the schedule, I think for the ones made in August the first one we come across is Lot 17, so I hand you now your files for Lot 17 in Tract 13163, and ask you to state what your card indicates with regard to the lease situation. A. No lease.

Q. On either unit?

A. That is right. [360]

Mr. Axelrad: Your Honor, could I interrupt a minute to ask a question?

The Court: You may.

Mr. Axelrad: If Mr. Chehock will tell me what the purpose of this is, perhaps we could stipulate. He has never asked me, to my knowledge, about anything on this. I haven't the slightest idea what he is getting at. I think this is a terrific waste of everyone's time.

(Testimony of Philip Pierre Boland.)

Mr. Chehock: The purpose of this is I would like an explanation of how it come to happen that on all the escrow instructions for these properties placed in escrow in August, there is a designation that there is to be a signing date subsequent to September 21, 1946, and on the others there is not.

Mr. Axelrad: Why don't you ask the witness?

Mr. Chehock: I want the record first to show what the facts are, and then I will ask the witness.

The Court: Well, if it is a matter of getting what the records show, I think that can be done as well by reading into the record as by asking the witness.

Mr. Axelrad: If Mr. Willkie, who I think has gone through these, the Revenue agent, will state that is what they say, I will stipulate to it. I don't see any point in this. I have never been asked to stipulate on it.

The Court: How many more of them have you got of these in August?

Mr. Chehock: There is quite a group of them, your Honor.

The Court: You don't have all of them there?

Mr. Chehock: I don't have all of them here.

The Court: Finish what you have got there. Is that what you picked out?

Mr. Chehock: These are the ones I picked out, yes, your Honor.

The Court: Then you can finish those.

Mr. Chehock: This is a fair criterion, I think, of what they show.

(Testimony of Philip Pierre Boland.)

The Court: Well then, let's get along.

Q. (By Mr. Chehock): I refer you now to your files for Lot 21 in Tract 13163 and ask you what your cards indicate as to whether there was any lease. A. No leases.

Q. On either unit? A. That is right.

Q. Does the escrow instruction have a signing date for the Murphys and Pools? A. Yes.

Q. What does it say?

A. Signing date 9-26-46. [362]

Q. Does that correspond, then, with the *grand* deed date? A. No.

Q. Well, doesn't it? A. No.

Q. Isn't 9-26-46 the same as the grant deed date?

A. I thought this was 9-23. Excuse me. That's right.

Q. Doesn't that correspond with the grant deed date? A. That's right.

Q. I refer you now to the cards for Lot 28 in Tract 13163, and ask you what your cards indicate as to the lease situation at the time of the sale.

A. No lease.

Q. On either unit? A. That's right.

Q. I ask you if there is any designation for signing date there on the escrow. A. 9-26-46.

Q. Does that correspond with the date of the grant deed? A. That's right.

Mr. Chehock: I think, your Honor, I could go on. If counsel wants to pick out any one he wants to in August, I will be glad to go through it, but

(Testimony of Philip Pierre Boland.)

I don't see any necessity for going on further to prove this point. [363]

The Court: It is your case.

Mr. Chehock: If counsel doubts it is the situation, I will be glad to put out any one that is placed in escrow in August, if he will call it out.

The Court: Well, he will let you know what he wants.

Q. (By Mr. Chehock): Mr. Boland, can you state why on these other properties they do not have this typed designation for the signing date, apparently for the grant deed, while on these here it does have that? A. No, sir, I can't.

Mr. Axelrad: I did not hear the answer.

The Court: He said he couldn't explain.

Q. (By Mr. Chehock): Do you know who put those on there? A. No, sir.

Q. They are your files, aren't they?

A. The envelopes are mine. The files evidently were mine. At the time that I was there, they were mine.

Q. Did you have these printed deeds for Tracts 11451 and 13163 printed, or who had those printed, do you know?

A. I think I called the attorneys that had been doing the work for Artcraft, and had them get the deeds printed. I am not definitely sure about that. [364] I think I had somebody order them printed, yes.

Q. Do you know who printed them?

A. No, I don't remember.

(Testimony of Philip Pierre Boland.)

Q. Do you know when you had them printed?

A. I had the 70, the ones for the first ones, printed shortly after I started, I think at the suggestion of the Bank of America.

The Court: Let me see one of them.

The Witness: And the others when they finally decided to sell the 100 duplexes.

The Court: All right. Go ahead.

Q. (By Mr. Chehock): Now, the deeds, the forms that appear in Exhibits VV and WW, were the form deeds used in the sale of the 70 and the 100 duplexes, that is right, isn't it?

A. That's right.

Q. Wasn't there a large sign that Artcraft manor duplexes were for sale at the corner of Stearns and Lakewood Boulevard?

A. I don't remember.

The Court: What was the answer?

The Witness: I don't remember any sign there.

Q. (By Mr. Chehock): How many duplexes did you have for model duplexes?

A. We used whichever one was vacant. [365] whichever one didn't have a tenant in it, we used that as a model. They all looked alike, you know. I would say, "Go look at that vacant one and see if you like it and then just go out and pick any one out up and down the street."

Q. Who would have access to this copy of the escrow instructions that you have on the matters I have just questioned you about on the signing

(Testimony of Philip Pierre Boland.)

date that would have had the date typed in there?

A. I don't know.

The Court: It is probably in the record, but just to give me a present picture and just in case it isn't in the record completely, state again, just give an account as to generally where these escrow agreements originated, who handled them, from the time they started until they were completed and filed. Start with this situation. You are down there. You have been down there at the property and one of these people that you told to go up and look at a vacant one comes back and says they want a certain one.

You go over whatever the preliminaries are. Now you are ready to start getting these papers in shape and taking the initial steps to complete the transaction and delivery of the deed through escrow to the individual.

The Witness: I would fill this out.

The Court: What is that?

The Witness: That is the first step. [366]

The Court: That is the contract?

The Witness: That is the deposit receipt. It is the contract on the purchase.

The Court: All right.

The Witness: Then I would have either Mrs. Woodruff or the girl that worked for me, if I were too busy, to fill out a statement of identity and take their credit information, where they worked; then I would take this information that I had received from the purchaser, plus this——

(Testimony of Philip Pierre Boland.)

The Court: Plus what?

The Witness: This order blank.

The Court: All right.

The Witness: I would put them in an envelope. The next day, or as soon as I could, I would take them to the bank. The bank had a setup to take case of the rest of it, of the entire escrow.

The Court: What happened about the escrow?

The Witness: Then when they reached the bank, the information would be sent to the bank by the credit department.

The Court: All right. Then what?

The Witness: Then they would proceed with the rest of this, to fill out the escrow papers.

The Court: The escrow papers?

The Witness: Yes. [367]

The Court: Who would?

The Witness: The bank.

The Court: Yes, and then what?

The Witness: They had received one blanket instruction from me at the beginning as to what I wanted done on these.

The Court: You gave them a pattern?

The Witness: That's right. Then I was through with the thing.

The Court: You never had anything more to do with it?

The Witness: The only time I had anything more to do with it was when they did not go down to pay their money, their impounds, or they didn't

(Testimony of Phillip Pierre Boland.)

go down to sign them, I would have to get after them and have them come down.

The Court: You were interested in whether or not they would go through?

The Witness: Yes.

The Court: And whether they were closed out?

The Witness: That's right.

The Court: What did you do about that?

The Witness: If they are canceled out, which in many cases it happened, about 100 per cent, I mean at least half of the time, you would have to sell them over again, so I would take the papers, [368] tear them up, put the card back in, and start all over again.

The Court: Did you ever go to the bank on the others?

The Witness: Oh, yes, I would go down to the bank every day or every two or three days, whenever I could get to it.

The Court: But you didn't have any dealings with any of the individuals on getting the escrow papers in there?

The Witness: No, not after I took the order down to the bank. They handled it from there on.

The Court: All right, go ahead, Mr. Chehock.

Q. (By Mr. Chehock): When did the duplicates for the escrow instructions come back to you so you could put them in your file?

A. I don't know.

Q. Well, you got them all.

A. I don't remember putting them with these

(Testimony of Philip Pierre Boland.)

files. They probably came back after I sold them and was gone. I am not much of a bookkeeper. I had somebody else take care of it, and I didn't pay much attention. My job was to sell and keep them sold. The details were to be taken care of there, in escrow. If they came back and I had to sell them again, that was that.

I imagine some of them came along at different times, but after six or seven years, you don't [369] remember when certain ones come back.

Mr. Chehock: I think that is all, your Honor.

The Court: Any questions?

Mr. Axelrad: Yes, I have a few.

Redirect Examination

Q. (By Mr. Axelrad): I hand you one of these envelopes that you were referring to under cross examination. This one just happens to be Lot 8, Tract 13163. Mr. Chehock referred to these throughout his cross examination of you as your files. Was this envelope yours?

A. It was up until the time I was selling them, I mean until they were sold and finished.

Q. Did you have these in your possession after you left?

A. No. When I left, I left them there.

Q. Left them with whom?

A. Left them at the office where they were sold from, Arteraft's office.

Q. This card, you say you had typed up?

A. That's right.

(Testimony of Philip Pierre Boland.)

Q. For what reason?

A. I kept them in a little index box. Whenever I would sell one of them, I would pull the card out.

Q. This particular one has a lot of writing on, [370] this first one, 2228 Grand Avenue. It says, "No lease." Is that your handwriting? A. No.

Q. The second one, 2230 Grand Avenue, it has a date of 11-9-46. Is that the correct date?

A. Yes.

Q. What do you suppose that signifies?

A. I suppose it had to do with the termination of the lease.

Q. Do you know that? A. No.

Q. Is that your writing? A. No.

Q. There is written on here in blue pencil the word "sold." A. That is my writing.

Q. That is in your writing? A. Yes.

Q. Then there is printed something.

A. That is my printing.

Q. Then way down at the bottom of the card, there is something in pencil. Can you read that?

A. $2,750.00 down.

Q. Is that your handwriting?

A. Not my handwriting. It is one of the girls.

Q. Do you know what it signifies?

A. Probably the down payment on this particular deal. I am not sure.

Q. Another paper in this particular report is a character and credit loan report. Is this part of your files?

A. That came from the credit association, and

(Testimony of Philip Pierre Boland.)

then the original went to the bank. A copy came to my office, yes.

Q. Is it customary, if you know, in a real estate transaction, for the broker to get a copy of the deed? A. No.

Q. Is this grant deed a copy of the deed closing this transaction? A. I think so.

The Court: There isn't any *doubt it,* is there, Mr. Axelrad?

Mr. Axelrad: I don't think so, but I want to find out if this is his file, and I don't think it is. I don't think any part of this is his file except the card.

The Court: For the purpose here, does it make any difference whether it is his file or Mrs. Woodruff's file? They were papers that carried through the transaction here. No one has ever questioned they weren't, and there is every reason to believe they were, so there isn't any reason to quibble over this sort of matter. Part of this is his file [372] that he worked from. The others show what they show.

Mr. Axelrad: Your Honor, all through the cross examination of him, this was referred to, not once, but I would say a hundred times as his file, and I am trying to show a very small part of this was his file and nothing else.

The Court: All right. The record shows that and I have asked him myself to clear up how these things were handled, so let's move along on to things that matter.

(Testimony of Philip Pierre Boland.)

Q. (By Mr. Axelrad): Were you ever given any instructions by Mr. Pool or Mr. Murphy about delaying the escrow? A. No.

Q. This typewriting you saw on these various escrow instructions with respect to the signing date, was that a carbon like the rest of the copy, or was that typed in original typewriting?

A. It was typed in fresh.

Q. And you don't know who did it.

A. No.

Q. Or do you? A. No, I do not.

Q. When the 70 houses, when arrangements were made about the 70 houses, I think you left the impression on cross examination that something was said about the 100. Would you please [373] explain just exactly what was written in the letters you mentioned, insofar as you remember? Who instigated the writing? A. I did.

Q. What were you offering?

A. Murphy asked me to put it down in writing so he could go over it, so I wrote down what I thought could be done with the entire tract and how much I could get for it.

Q. For the entire tracts? A. Yes.

Q. The 100 and the 70? A. Yes.

Q. What was written back?

A. If I could do that, and they agreed to the certain terms I had set out, it would be satisfactory to him.

Q. Was there anything in writing about the 100 as well as the 70?

(Testimony of Philip Pierre Boland.)

A. I mentioned I wanted to sell it all.

Q. What did they say?

A. He didn't mention that. He just mentioned to answer the price which I could get would be satisfactory, providing he could prevail upon Pool, or I could, to have him sell them.

Q. Did you prevail upon Pool to sell the 100?

A. No, not at that time, definitely not.

Q. When was the first time you ever got [374] permission to sell the 100 houses?

A. It would have to be after the 15th of July, because that is when I came back here from a trip.

Q. The 15th of July of what year?

A. 1946, because I was married the 6th of July back in the Middle West. I got here about the 15th.

Q. What particular problems in selling the houses and these apartments or duplexes, or houses, existed with respect to occupancy?

A. Well, the lease didn't mean anything so far as the owner is concerned.

Q. What do you mean by that?

A. I mean there was no arrangement made. He wasn't allowed to take the last month's rent. If they wanted to move out, they could move out. So far as I am concerned, I didn't pay any attention, didn't care whether they were leased or not. I was interested in having them become vacant as fast as possible. But some ran into trouble on that, because the rent control wouldn't let them get them out even after I sold them.

So as soon as we could, where there was no

(Testimony of Philip Pierre Boland.)

lease on and it was on a month-to-month basis, we could get them vacant or get it so the owner could get in, and we tried to arrange that plan. Some people bought them while they were occupied and waited several months, even five or six months, [375] before they could get in. That was the big trouble that we had there, to find a place for them to live until they got out.

Q. Would it be correct to say it was more difficult to sell one that was occupied than it was to sell one that was vacant? A. Yes.

Q. Did most people want to occupy them?

A. Yes. They wanted some place to live.

The Court: There were very few places that were unoccupied?

The Witness: Yes.

The Court: And if they were, they weren't unoccupied very long.

The Witness: Yes.

Q. (By Mr. Axelrad): Do you know in round numbers whether there were many or few that were under lease in either the 70 or the 100?

A. I didn't pay any attention. I didn't care. I was anxious to sell them regardless. I knew they would sell.

Q. Didn't it mean something to you——

The Court: What is all this that we have had about whether they were under lease or not for? We have testimony, first, that they were leased, all of them, for a term of a minimum of one year. Then when certain information came along, they

(Testimony of Philip Pierre Boland.)

didn't renew them. They would allow the lease to [376] expire, and as the lease expired, they weren't under lease any more. Does it make any difference about the dates on which those original leases expired?

Mr. Axelrad: I think, your Honor, that counsel for the Respondent has some theory, because there were no leases after a certain date in 1946, that it must have been because they intended to sell them all. The testimony, I think, consistently shows the contrary. But the difficulty with that, and the Petitioner has it in any case, is in knowing how much of any given testimony the Court is going to accept as such. A lot of this has to be cumulative and repetitious because it seems to me you might decide that one witness is right and another one isn't. I don't know.

The Court: And after you accumulate and so forth, I may do exactly that after it is all over.

Mr. Axelrad: I am only trying to do the best I can.

The Court: My query wasn't critical of you in any sense. I was trying to arrive at the problem.

Mr. Axelrad: That is the problem.

The Court: As to why we had to proceed further. I haven't heard any reason yet. Maybe counsel for the Respondent has some reason. My query was directed to both of you, not to you alone.

Mr. Chebock: I would say there are two, at [377] least, major reasons for this that we have. One is to show that they had a general pattern of

(Testimony of Phillip Pierre Boland.)

activity of obtaining the leases on or about the same time as they acquire the 100 duplexes.

The Court: Who acquire?

Mr. Chehock: Murphy and Pool.

The Court: You mean as they got the deeds from the corporation?

Mr. Chehock: Right. There is very little lapse of time there.

The Court: All right.

Mr. Chehock: Certainly, the fact that there were no leases made and the fact that as cancellations came on they made no written leases, is evidence we can show as to the situation at the time of the sales and is further evidence of the fact that they are out of the rental business and in the business of selling houses, holding them for sale.

The Court: You can argue that. I will be perfectly frank. I don't think it means very much, for this reason: Under rent control, about the only way a tenant could be ousted, if he was fairly decent and paid his rent, was to have someone buy the place from under him and want to live in it, and then they met with some difficulty. I imagine when he got behind with his rent, it would take a little bit of time to deal with that. [378]

I can't see that there would be any reason for having leases where the places were occupied or the rental rate, rather, was established when the tenure was for an indefinite duration, and, of course, there was the problem of controls, the possibility of controls going off.

(Testimony of Philip Pierre Boland.)

Mr. Chehock: If controls did go off and if they were on a month-to-month proposition, they would be able to oust them for purposes of sale better than on a long-term written lease.

The Court: Oh, yes. So whether they wanted to sell or whether they wanted to continue, they were better off without a lease from most angles, it would seem to me.

Mr. Chehock: Well, it seems to me that they——

The Court: Now, from the selling standpoint, selling was one way some tenants were ousted. They could find people that wanted to buy a place to live in and make it their home. We had a lot of big publicity in Washington about Senator Daniels of Texas. He ousted a lot of people out of the apartment house he bought, because he said he had a big family. Some of the columnists and commentators thought that was sort of a hatched-up idea, that he didn't have to have all that for his home.

Of course, what the facts are on that—I am not representing him, but just giving this is an illustration of things as they appeared in the public [379] press—for his own purposes, whether political or otherwise, he responded with a showing he did convert that apartment house to a family home, and on the face of it made a pretty good representation. But he got all those tenants out of there because he bought it to live in.

So I just wonder if there is any need of going on here. We see what the general pattern is. The Petitioners have testified that they had leases, that is,

(Testimony of Phillip Pierre Boland.)

shown that they had leases, but after a certain time they didn't get leases any more. They let them run out, and then after they had run out, they continued without leases.

The Witness: Could I volunteer a statement, your Honor?

The Court: No, you may not.

Mr. Chebock: It seems to me, your Honor, that the magnitude of the situation, the fact that the evidence will show, when we present it, that at the time of the sales there were only 41 of the 200 units of Tract 13163 that were under lease, is significant.

The Court: If you tabulate that and want that to appear as of record, why, then that is perfectly all right, to have it appear of record, and you can reason from that in whatever manner you think is proper and correct.

Counsel, on the other hand, will reason what he thinks it means in the light of what his evidence is.

All I am interested in is what the fact is, and the fact is that as of the dates they were thus and so, and that is something that can be tabulated from these leases or these papers or these cards. I don't care what it is. I just wonder about all this tedious sampling, because in the end, unless I get a complete tabulation, I wouldn't know whether what you are saying is right or not.

Mr. Chebock: I would rather get this information out of Mr. Boland, since they are his cards, but the records are voluminous and he is not in a

(Testimony of Philip Pierre Bolard.)

position to testify that way, so I am giving a sampling to show the reliability of what the agent is going to testify to.

The Court: Actually, whether you get him to read it off or not, the information you are getting is coming off these cards.

Mr. Chehock: All right.

The Court: And the evidence is there in the cards.

Mr. Chehock: All right.

The Court: All the evidence is in that stack of leases.

Mr. Chehock: All right, your Honor.

The Court: So let's get it off of that. I never did see much reason for doing a question and answer job in the course of a trial where all you are having someone do is read from the records, [351] when, rather obviously, the information they were giving was not their own, but the card information or paper information, and those things we can tabulate.

All right. If you want the last question you asked, we will have it read and then you can go along with the examination of the witness.

(The record was read.)

The Court: Now, you had some observation to make?

Mr. Chehock: I just want to make this comment to the Court in regard to that, and that is I think the evidence is they continued to lease these 22 even

(Testimony of Philip Pierre Boland.)

beyond this period, but not the 170, and that enters into the picture.

The Court: All right. That would be a matter of record. You can put that in and make your argument on it, and then after I see what the evidence is there and read the arguments and do my reasoning, I will come out where I think I should.

Mr. Chebbck: All right.

The Court: All right. You may go ahead.

Q. (By Mr. Axelrad): Did you advise Mr. Murphy and Mr. Pool that they shouldn't take any more leases after you first started talking to them, or at any time?

A. I don't think it would ever come under the heading of advice. We discussed it, and from the [382] standpoint of an owner, there was nothing for him to have a lease that meant nothing to him and only meant something to the tenant, so you couldn't raise the rent and couldn't get him out.

Q. But did you specifically recommend that, looking to your sales possibilities?

A. Yes. I didn't want them leased.

Q. What did you tell them?

A. I told them if they were not leased, it would be better, as far as the chance of having them vacant, or to have them vacant, if you sold them.

Q. With respect to the 70, did you advise them, when you started to sell, not to sign any more leases, or didn't you?

A. I don't remember anything definite on that. There were just two vacancies at the time.

(Testimony of Philip Pierre Boland.)

Q. Two vacancies?

A. In the entire 70 units, when I started selling them.

Q. The rest were occupied?

A. The rest were occupied.

Q. But you don't know whether they had leases or not? A. No.

Q. Did you have transactions where the lease had to go into escrow? If there was a lease, that would be an escrow paper? A. Yes. [383]

Q. You would have to sign the lease?

A. Yes.

Q. Were there a number of those?

A. I think there were a limited number.

Q. A limited number? A. Yes.

Q. In the 70? A. Yes.

Q. And what about the 100?

A. I think there were some there, too.

Mr. Axelrad: That's all.

Recross Examination

Q. (By Mr. Chehock): Mr. Boland, let me ask you this question: As vacancies occurred in the duplexes, both as to the 70 and the 100, and you had them for sale, did you leave them vacant from then on, or did you rent them to new tenants?

A. Generally, if it were possible, I kept them vacant. In several instances I let people who had bought one live in somebody else's that was vacant until they could get in their own.

Q. There were a number of cancellations during

(Testimony of Philip Pierre Boland.)

this period that you were selling the 70 and the 100, weren't there?

A. Cancellations of what? Of orders? [384]

Q. Of leases, of folks moving out.

A. Some.

Q. Your procedure there was to leave those vacant? A. Sure.

Q. So it would help you in making sales?

A. Naturally. The person buys because he wants to get in there.

Mr. Chehock: That's all.

Mr. Axelrad: That's all.

The Court: You are excused.

(Witness excused.)

Mr. Axelrad: Mr. Lampe.

Whereupon,

ERWIN LAMPE

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your full name for the record, please?

The Witness: Erwin Lampe, L-a-m-p-e.

Direct Examination

Q. (By Mr. Axelrad): Mr. Lampe, what is your profession or occupation?

A. I am a certified public accountant and do a lot of tax work. [385]

(Testimony of Erwin Lampe.)

Q. Were you a certified public accountant for Artcraft? A. Yes.

Q. For what period of time?

A. Beginning in about February of 1943, Mr. Joe Smith, who was then the president of Artcraft Builders, came to me at my office, which was then at 650 South Spring Street, and at that place I was associated with the firm of Claude Parker. Mr. Smith's brother had been a client of the firm for some time, and he came in and asked that I audit the books and make up the tax return for Artcraft Builders, Inc.

Q. What was the business of Artcraft at that time?

A. At that time they were building individual homes on order for resale.

Q. Did that business change while you were the auditor?

A. Yes. The building of individual houses ceased, I think, with 1942 building operations. Then there was a period in which there were no building operations, and thereafter Artcraft built only for the account of Pool and Murphy.

Q. What happened to Cooke and Smith?

A. Mr. Pool and Mr. Murphy apparently wished to go on and to build houses for rental purposes for war work. Mr. Smith and Mr. Cooke—incidentally, Mr. Cooke being Mr. Smith's son-in-law—took the position that the building of [386] rental units involved too great a risk. As a result of numerous

(Testimony of Erwin Lampe.)

talks, Murphy and Pool bought out Smith and Cooke.

Q. Did you do the auditing for Pool & Associates when they were formed?

A. Yes. During all this period—I would like to explain for the record—that I was in the position of managing accountant, and when I say I did audits, a good deal of the detail work was done by my men and then submitted to me for approval, but that the reports were all over my signature.

Q. What was the firm name under which you worked?

A. Until November 15, 1945, I was associated with Claude Parker, and those reports were signed "Claude Parker, by Erwin Lampe, Certified Public Accountant."

November 15, 1945, I associated myself with Arthur Young & Company. Immediately I was in the office simply as an employee with a bonus contract, but I had the rights of a partner as far as signing reports.

Q. All right.

A. I did not become a partner of Arthur Young & Company until January 1, 1947.

Q. Who did the actual book work? You said you were sort of manager and you checked on them, but who did the leg work?

A. On the first audit, the audit was made by a man [387] named George Clark. Shortly thereafter, because he found that in the 1942 books, which had been maintained by Mr. Cooke, that there

(Testimony of Erwin Lampe.)

were a vast number of errors, Mr. Pool asked me to release Clark to them. Because accountants were very scarce, I stalled for several months, and I think it was in May of 1943 I released Clark after I had gotten them to increase the salary that they were offering him.

Q. In checking on the audits of Edward Pool & Associates, did you have to verify the date on which they took title to these various properties?

A. I did.

Q. Why would you have to do that?

A. When one company, Artcraft Builders, had done the building and then transferred these properties to the four people for whom tax returns and reports were made under the name of Edward Pool & Associates, the date of transfer is an important date.

Particularly, a question arose as of February 1, 1946. The properties referred to as the 100 units, or 100 properties here, were set out in the books and in the minutes as having been transferred on February 1, 1946. When my man came in with those working papers, there was no notation that he had examined the actual deed. I knew Phil Swaffield of Long Beach, who was the attorney for Pool and Murphy, and for Artcraft Builders, quite well, and I called him on the [388] phone and asked him about it. He told me——

Mr. Chehock: Just a minute. I object to what he testifies he told him as hearsay.

Mr. Axelrad: Your Honor, even if it is hearsay,

(Testimony of Erwin Lampe.)

in this case the man who told him is dead, and I think it would come in under an exception to the hearsay rule.

The Court: What was Swaffield's position?

Mr. Axelrad: He was the——

The Court: I am asking the witness.

The Witness: Phil Swaffield was the attorney for these people and was under a monthly retainer by them during the period.

The Court: Had you been advised by Pool and Murphy that Swaffield had that position with them?

The Witness: I had.

The Court: Had you been authorized to take up matters relating to their affairs that were within your province, your employment, with him?

The Witness: I had.

The Court: Go ahead.

The Witness: I called Mr. Swaffield and asked him where the deed was. He said that the deed had been executed and had been mailed to Pool and Murphy.

On his word that it had been executed, I passed the deed and signed the report. [389]

Subsequently I discovered that that particular deed apparently was lost and a new deed executed on March 21, 1946.

Q. (By Mr. Axelrad): This deed that you say was apparently lost concerned the 100 duplexes?

A. That is correct.

Q. And then you say that the word Mr. Swaffield gave you was that it was executed when?

(Testimony of Erwin Lampe.)

A. That it was executed—and I have had to refer to notes on this—it was executed either February 1st or February 2nd, as of February 1st.

The Court: We will take a brief intermission.

(Short recess taken.)

Q. (By Mr. Axelrad): What was the arrangement, what employees did Edward Pool & Associates have? You made up their returns and kept their books, audited their books. Did they have any employees listed?

A. They had no employees, as such.

Q. What kind of an organization were they?

A. The organization started out with four people, each buying an undivided one-fourth interest in the site for a business block on the corner of Stearns and Lakewood. They kept accounts or, rather, they employed Artcraft Builders [390] to keep their accounts and to collect their rents. They had no employees of their own.

Q. Did they have any activity of their own whatsoever other than the occasional buying of some property?

A. They were strictly in the business of holding property for rental until such time as they started liquidating in 1946.

Q. Did they have any formal partnership agreement, or agreement of any other kind?

A. No. There was not partnership agreement.

Q. Was there any discussion that you had with the Associates about the time they were deciding to

(Testimony of Erwin Lampe.)

acquire these duplexes, about whether they would be sold or held for rent?

A. Considerable discussion with both Mr. Murphy and Mr. Pool at the time of the first contract, which I think was in October of 1943, and in which they agreed to take the first group of buildings over from Artcraft.

At that time all the discussion was in connection with holding these for rental, and they did raise the question at that time, or sometime later on, as to whether or not I thought they might not be in trouble renting these things to Navy people instead of strictly to defense workers, and I told them I didn't think anybody would have the gumption to prosecute a person for renting a house to somebody on [391] active duty, but that that was a law question and they better hunt up their lawyer.

Now, as far as selling houses was concerned, about May 1, 1946,—no. When I prepared the reports of Artcraft Builders for the year ending December 31, 1945, and of Edward Pool & Associates for January 1, 1946, I went over the figures with Mr. Pool and Mr. Murphy and made it a point to emphasize to them that while the figures showed a rather substantial rental income, that, actually based on market values as they stood at that time, early in 1946, the income really represented no return at all on the current real estate value of houses.

Q. Did you make a study of what the market price of similar kinds of property was?

A. I did.

(Testimony of Erwin Lampe.)

Q. Was that part of your duties?

A. I thought it was part of my duty because I was taking care of their personal returns as well as their audit reports, and perhaps I have always reached out a little past the mere making of audit reports in my work. As a matter of fact, you might say I volunteered that information to them. They asked me at the time if I thought they should diversify their investments. I told them that I was not going to make any definite recommendation as to whether they should sell or what they should do, that they must make up their own minds, [392] but that in view of the figures, it looked as though the then market for real estate was too high. I think I might have been wrong on that, but that is the way the figures looked at that time.

Q. Was it the expectation that something would happen to the market after controls went off, that there would be a change one way or the other?

A. Not after controls went off, but you had a peculiar situation arising here in California. There was much building during the war, a vast increase in manufacturing, and an expected decline sometime after the war in rental and housing values, which did not materialize. There was a short dip in the real estate market after September, and then a very, very *sharp in* all types of housing values.

Q. And the rise was not expected before it occurred?

A. All of the people whom I had originally considered experts in real estate were caught. I was

(Testimony of Erwin Lampe.)

not smart enough to see it myself, and I thought at the time I was somewhat of an authority. The best rated man in Southern California on housing and rentals and loans at that time, who was a Mr. Dutcher, who was the chief loan man for the Bank of America, he didn't buy any property. We were too conservative.

Q. You say you made up a report of some kind. What did that show with respect to this property, specifically? [393]

A. The report I made up was just a regular audit report showing regular income; a regular report.

Q. Regular income and expenses report?

A. Yes, regular income and expenses in dollars.

Q. You say you did something in addition?

The Court: For whom did you do that?

The Witness: I did that for Artcraft Builders, which was a nominal report for Ed Pool & Associates, the four people who owned this property, because the figures in themselves, while correct, did not tell the whole story. I took it upon myself to consult with them and advise them of my feelings on the matter.

The next contact I had with them was about May 1st or May 2nd of 1946, when Mr. Murphy came into the office. At that time I was with Arthur Young & Company and my office adjoined that of Mr. McTavish, who was the senior partner here.

Q. (By Mr. Axelrad): When was this, you say?

A. About May 1st or May 2nd of 1946.

(Testimony of Erwin Lampe.)

Q. What occurred then?

A. Mr. Murphy came in and talked to the two of us and told us that he planned on trying to liquidate part of his holdings, to diversify. He said that he had made arrangements with Mr. Boland to do everything that there was [394] to do in connection with the sales, that he was going to liquidate for cash only, and he asked the question if we would consider this as a capital gain.

Mr. McTavish, who was my senior in the organization, said very strongly, "Why, there is no question at all." Because I concurred in it, I didn't say anything at that time.

The Court: What was it Mr. McTavish told them there was no question about?

The Witness: No question about his falling in a capital gain if he did sell some of the houses on the basis Mr. Murphy outlined.

The Court: All right.

Q. (By Mr. Axelrad): Did Mr. McTavish have any facts on which to state that?

A. He had been over their reports with me. He knew how long the property had been held. He knew the circumstances and the background, and he had Mr. Murphy's statement as to how they were going to sell them, the reasons for selling them.

Mr. Murphy told him Mr. Pool and he were turning over the whole sales over to Mr. Boland, that they were going to sell exclusively for cash and they wanted no part of any seconds or any hangover

(Testimony of Erwin Lampe.)

on the property; they wanted to liquidate and get in the stock market.

The Court: Would that make any difference, whether [395] they sold for cash or credit?

The Witness: It seemed to me if you were liquidating, to me it seemed to make a difference.

The Court: All right, go ahead.

Q. (By Mr. Axelrad): In your audit of both Artcraft's books and the Associates' books, did you have an opportunity to know what Artcraft was being paid for serving as a rental agent? I don't want to know the amounts. They have been stipulated. Did you have an opportunity to see that?

A. Yes, I did.

Q. Was there ever any discussion about how the amount should be fixed?

A. No; except that sometime after Artcraft had started to act as rental agent for Edward Pool & Associates, I was asked about it, and I told them I wouldn't fix a figure, that they must fix it and try to fix it at as fair a price as possible, as though they were dealing with an outsider.

The Court: You mean this fee and so forth was fixed after?

The Witness: No, the fee was fixed by Ed Pool & Associates immediately after they started this business of having Artcraft act for them. [396]

The Court: When was that?

The Witness: In the latter part of 1944, I think it was.

Q. (By Mr. Axelrad): That was after they got,

(Testimony of Erwin Lampe.)

the Associates got title to the 22 apartments and the 70 duplexes? A. That is correct.

Q. Did they continue to pay a fee regularly?

A. They paid a fee.

Q. Arteraft collected all the rents?

A. That is correct.

Q. And then what did they do? Pay the expenses?

A. They collected the rents, paid the expenses, took care of the upkeep, in some cases paid the utilities, and turned the net over to Edward Pool and Associates.

Q. After first deducting their fees?

A. I think that is correct. In every case—there were settlements back and forth between the two parties, but I think in every case—it was not done on a regular monthly basis, but they did deduct their fee.

Q. Are you familiar with an incident that previous testimony indicates occurred in 1945 with respect to refunding the last month's rent that they had taken as security?

A. I am familiar with it only to the extent I know something along that line happened about that time. [397]

Q. The books showed it, did it? A. Yes.

Q. A refund or a credit.

A. The books showed some refunds of rentals which had been received as the last month's rent on leases.

Q. Did you visit the office at all, that is, Art-

(Testimony of Erwin Lampe.)

craft's office at all during the time that these properties were being liquidated; were you ever there during that time?

A. I was there once in August, the latter part, I think, of August, 1946. During the early part of the summer I had spent some time in San Diego helping Ryan work out their termination claims against the government, and in the latter part of August of 1946, I drove down there to see how things were going with them.

At that time there was nobody there except Mr. Boland, and I think Miss Woodruff in the office. Mr. Murphy was fishing some place, and Mr. Pool, I was told, was back in Cincinnati.

I simply looked around to see how things were going and talked with Mr. Boland, and he said sales were going good, and suggested that he had another deal on involving his own work, that he might have an accounting job for me. But that didn't go through.

Q. Did they ask you any advice as to when they might sell the 100 duplexes and get favorable tax treatment? Was [398] that ever discussed?

Mr. Chehock: Your Honor, this is all hearsay.

The Court: You may answer.

The Witness: To the best of my knowledge, no.

Q. (By Mr. Axelrad): Were you the only one, you or Mr. McTavish, the only one purporting to give the tax knowledge, to your knowledge, tax information, I mean?

The Court: I think that is not a good question.

(Testimony of Erwin Lampe.)

Mr. Axelrad: Let me rephrase it, your Honor.

Q. (By Mr. Axelrad): Were you asked from time to time—you did prepare the tax returns, did you testify? A. I did prepare the returns.

Q. Did they ever ask you tax questions?

A. They did.

Q. Did they ask you specifically about the 100 duplexes?

A. No. I remember that when I found out they were selling the 100, I was a little disturbed, because I didn't find it out until October or November of 1946, because they had gone ahead without consulting me. I am not certain as to the date when that date was, whether it was October or November.

Q. But you are certain you didn't give them advice one way or the other about the 100? [399]

A. No.

Q. You didn't ask them to delay selling them for any certain time?

A. No, because I didn't learn until the audit was made at the end of the year 1946 that this deed had not been recorded until February 1, I mean that this February 1 deed was not a good deed. Subsequently, I learned that that deed had been lost and the new deed issued in March.

The Court: You didn't know whether the February 1st deed was good or not, did you?

The Witness: No, except I had made a report stating that the property had been transferred as of February 1, and I thought I had done everything

(Testimony of Erwin Lampe.)

necessary to satisfy myself properly that that report was correct.

The Court: Were you going under the assumption that the mere fact a deed might be lost would make it no deed?

The Witness: No, because they had been talking here about a September 26 date, which would have some relation——

The Court: I am not asking you about that.

The Witness: No. I would assume it was a good deed. I still assume that these properties were first transferred on February 1, 1946. [400]

Q. (By Mr. Axelrad): In your income tax report for the Associates, did they pick up the income from that date on? A. They did.

Q. Did they start paying the fees to Artcraft from that date? A. Yes.

Q. So that Artcraft reported income from that source? A. That is correct.

Q. The books, therefore, and the income tax returns were filed on the assumption that they got title on February 1? A. That is correct.

Mr. Axelrad: That's all.

Cross Examination

Q. (By Mr. Chehock): Why didn't you know about the 100 duplexes being up for sale when you were down there in August, 1946?

A. As I say, that was a quick visit. I was down there to see if Pool or Murphy were there, and both of them were out of town. I had been in San

(Testimony of Erwin Lampe.)

Diego on a special job involving Ryan's tax work for the years 1943 through 1946.

The Court: Did you talk to Boland?

The Witness: I just talked to him for a few minutes about how things were going generally.

The Court: Did you know what he was doing down there?

The Witness: As a matter of fact, I had started out with the assumption that apparently everybody else had, that selling the 70 was going to take him a much longer time than it actually did.

The Court: Well, when he told you how things were going, didn't he tell you he had already sold the 70?

The Witness: No. All he said was the sales were going wonderful. I think he assumed I knew a great deal more about what was going on than actually I did.

The Court: Go ahead.

Q. (By Mr. Chehock): Why were you disturbed when you heard about the sales in October?

A. Simply that I thought I was losing contact with them.

Q. Is that all you were disturbed about?

A. That's right.

Q. You weren't disturbed about the holding period?

A. No, because I had always assumed that for my purposes the holding period certainly began on February 1, and probably would date back to March of—I think it was March or April of 1945,

(Testimony of Erwin Lampe.)

at which date they contracted to take these houses.

Q. The rent from these houses up to February 1, 1946 was reported as income for the corporation, wasn't it, Artcraft? A. That is correct.

Q. I refer you to Exhibit VV and ask you—Will you strike that, please?

I refer you to Exhibit WW, to the escrow instructions in that exhibit, and call your attention to the typing that appears below the place where the signature of the Murphys and Pools in the escrow instructions, on which is typed "Signing date 9-23-46."

Do you know who put that on there? And why it was put there?

A. I haven't the slightest idea.

Q. And when it was put there?

A. I haven't the slightest idea, sir.

Q. Do you know who would know?

A. No, I don't.

Q. At the time you advised them to sell these properties in—I think you said it was January, 1946, is that right?

A. I beg your pardon. I never advised them to sell any properties. I advised them at the present market value of their duplexes at that time, and if you figured in the depreciation and all of it, the present market value was then such that rentals under the fixed rates brought in [403] zero income.

Q. And by that you had in mind both the 70 duplexes and the 100 duplexes?

A. I was not referring to any particular rental houses, but simply that everything they owned was

(Testimony of Erwin Lampe.)

in rental units, and that rental units weren't returning anything on the present value.

What I am saying there is if you bought some stock for $100.00, and it had been paying $110.00, if the price increased to $1,000.00, and you point that out to somebody, they could make their own deductions, that if that rental income didn't go up, the price couldn't stay there indefinitely.

Q. What you are just saying has equal application to both the 70 and the 100 duplexes, doesn't it?

A. That's right.

Q. Now, isn't it also true that they continued to rent the 22? A. That is correct.

Q. Isn't that contrary to your recommendation to them?

A. I didn't recommend that they get out of the real estate investment rental business, but just that they shouldn't have all their eggs in that one basket, because the basket might fall apart.

The Court: According to your calculation, [404] it wasn't that, was it, but that the basket wasn't very good, according to your calculation?

The Witness: Well, that's right.

Q. (By Mr. Chehock): Did not Miss Woodruff work for both Artcraft and for Edward Pool and Associates?

A. To the best of my knowledge, she was always paid by Artcraft Builders.

Q. Who kept Edward Pool and Associates books? A. She did.

Q. Then wasn't she doing work for them?

(Testimony of Erwin Lampe.)

A. Yes, but she was an employee of Artcraft Builders and was reported on Artcraft Builders Social Security returns, and Edward Pool and Associates, the four individuals, paid Artcraft Builders a fee for services, and that was to include the bookkeeping.

Q. Well, Ruby Woodruff was paid by Artcraft, but she did services then for Artcraft, for Edward Pool and Associates, and for Mr. Boland, is that right?

A. What services she performed for Mr. Boland, I don't know about. For the other two, yes. Now, if you are asking me to testify as to whether she performed those services for Edward Pool and Associates, for them directly or as an employee of Artcraft, that is another question. She was never paid by Edward Pool and Associates. [405]

Mr. Chehock: That's all.

The Court: You are excused.

(Witness excused.)

The Court: Now where are we in this case?

Mr. Axelrad: Your Honor, I have two more witnesses. One is Mr. Pool, who is one of the Petitioners in this case. One is Mrs. Woodruff, who kept the books. The testimony that they can give is primarily all cumulative. In other words, the whole story is in so far as I know it, and both of them can confirm certain things. I don't think it should take too long.

The Court: How long do you think it should take, knowing what you are going to ask them, how long

do you calculate it would take for you to put in what you think you should from them?

Mr. Axelrad: I think the direct examination of the two of them shouldn't take more than 30 or 45 minutes in total.

The Court: Both together?

Mr. Axelrad: Yes, the total.

Mr. Chehock: I think the cross examination will be very short.

The Court: Is that all you have then?

Mr. Axelrad: That's all.

The Court: What do you have? [406]

Mr. Chehock: I just have one witness, the Revenue agent, with whom I will put in this schedule showing the data regarding the leases and the properties that were not leased at the time of sale. That should take just three minutes.

The Court: In that case, we ought to finish this before noon tomorrow?

Mr. Axelrad: We should.

Mr. Chehock: Oh, yes.

The Court: Then that would look like we would finish tomorrow. I was interested for two reasons. One is I wanted to look to my reservation. I didn't want to get caught with one and have to pay for it. The other is we have one more case and counsel are interested in knowing about when they might be reached.

So according to your best judgment, the time may vary, but according to your best judgment, the total time you think you will need, we should finish before noon?

Mr. Axelrad: I believe so.

Mr. Chehock: I don't think it should take any longer.

The Court: I think, then, it is so near 5:00 o'clock, we will adjourn until 10:00 o'clock in the morning. That means about two and a half hours for us to finish by noon. [407]

Mr. Axelrad: That is about the time that we can use.

The Court: Yes, that is how much time we would have before noon. From what I understand, you gentlemen think you would be comfortably within that time?

Mr. Axelrad: Yes.

Mr. Chehock: That is right.

The Court: All right.

We will come back at 10:00 o'clock tomorrow morning.

(Whereupon, at 4:55 o'clock p.m., an adjournment was taken until 10:00 o'clock a.m., Wednesday, March 4, 1953.) [408]

Proceedings

The Court: We will resume the Pool, Murphy and Artcraft Builders, Inc. cases.

Mr. Chehock: Your Honor, at this time I would like to present a schednle prepared by the Revenue Agent containing some five pages, and I should like to have it marked for identification.

The Court: Five pages as one exhibit. All right.

The Clerk: That will be Respondent's Exhibit III.

(The document above referred to was marked Respondent's Exhibit III for identification.)

Mr. Chehock: Could I have Exhibit HHH? I am referring now, your Honor, to the exhibit of five pages which has just been marked Exhibit III. I would like to state to the Court that this is a schedule made up by the Revenue Agent in which the third column, headed "Expiration date of regular lease in effect at time of sale," is a compilation of the information contained from all the cards on the 100 duplexes, such as is referred to in Respondent's Exhibit HHH, indicating as to whether or not there was a lease on hand at the time of sale and if there was the expiration date. That column is complete from the records.

The other two columns are headed, "Date of last one-year written lease," and "Date last written lease expired or was canceled." [411]

That information was obtained from the cards and from the leases of the Petitioners on hand and is complete as could be determined from the records available. There may be some discrepancies, but I think there are very few and that the Columns 1 and 2 are substantially correct.

The Court: What do you mean, there may be some discrepancies? Between what?

Mr. Chehock: All of the cards of the Petitioners don't seem to be available here.

The Court: You mean they are not all there?

Mr. Chehock: They are not all there. However, by working with these cards and by working with the cards that appear, such as Exhibit HHH, and

working with the leases and everything else, this is the information from the records that appears substantially correct.

The Court: Do you mean by that that since one set of cards, for instance, didn't have all the information, in order to get that information, you referred to some other card that you have mentioned?

Mr. Chehock: That's right.

The Court: And what you have on there in that instance would be from the other card? Some of the dates are from one card and some from another, because you had to look to another set of cards to complete your dates?

Mr. Chehock: That's right. [412]

The Court: All right.

Mr. Chehock: I would like a statement from Petitioners' counsel as to whether or not in his opinion this exhibit is substantially correct.

Mr. Axelrad: Well, I have naturally, your Honor, not examined all these cards, but I am willing to accept the accuracy of Mr. Chehock's statement. I would like to point out, however, the substance of what is on this chart has already been stipulated and it is really just superfluous, but I have no objection to it.

The Court: That is sometimes true, but where it is set up in tabulated form, it really helps all parties, because sometimes they would have to do it themselves, if they didn't, in the course of working on the case. While it is true that, strictly speaking, it is not primarily evidence, it is a summarization from matter that can be checked and verified,

particularly if it is covered by the record to just one step further along. So we usually welcome those things. It is subject to whatever question there might be as to accuracy, of course.

Mr. Axelrad: I am willing to accept it as accurate to the best of their knowledge.

The Court: All right.

Mr. Axelrad: That is satisfactory.

Mr. Chehock: The report is offered in evidence as [413] Respondent's Exhibit III.

The Court: It will be received, its nature and character being as stated in the course of the colloquy here.

(The document heretofore marked Respondent's Exhibit III was received in evidence.)

Mr. Chehock: Now, I would like to call the Court's attention to one situation I had in mind when I mentioned there might be something that appears as a discrepancy. The last lease on the address 2290 Grand Avenue, Lot 23, the expiration date of the written lease in effect at the time of sale in accordance with these cards, such as Exhibit HHH, for that particular lot would indicate that the lease expired March 31, 1947. The best records we could obtain from the cards was that the last written lease was made July 20, 1945. It was vacant on or about March 29, 1946, which would indicate in all probability by virtue of the fact that the cards, such as Exhibit HHH, showed that the lease expired on March 31, 1947, that would indicate that there was a lease made March 31, 1946.

The Court: Let me see it.

I notice that as to that date in the expiration date column, and with respect to the lot mentioned, there is a question mark alongside the date. Now, I understand, then, that your statement there is an explanation of what [414] that meant?

Mr. Chehock: That's right.

The Court: Now, I notice that there are one or two other questions marks here, and with the exception of one, the nature of the question mark, I think, is rather obvious, in that it shows and would indicate just an absence of record.

On the second page, however, there is one which is in form exactly the same as the entry opposite the property at 2290. Now, probably you better take that and state whether or not that same or a similar explanation is to be made. The others, I think, are very obvious. They just indicate the absence of anything.

Mr. Chehock: Your Honor, there are several instances——

The Court: The one I want to know is that one. I don't have any concern over the others. The one I am talking about is Lot 34 and the address is 2267. It in appearance is exactly the same as the one that you mentioned. I am not going to bother about the others, but I am going to ask for that one, becaue it is exactly the same as the one that you just explained. I am talking about 2267.

Mr. Chehock: All right.

The Court: The others that have question marks alongside are rather obvious, but that one, I want

to know if it is in substance the same as the one you just explained. [415]

Mr. Chehock: The one you made inquiry of, your Honor, is in substance the same as the explanation I gave on the other. I think that is the only correct answer to it.

The Court: I think for the purposes of this case it really doesn't make any difference.

Mr. Chehock: –No.

The Court: Because Petitioner has indicated that, generally speaking, along at about that time they decided to let the leases they had run out, and as fast as they would run out, why, they didn't sign any more. In some instances there up to that time, some of those where they were vacated and a new tenant came in, they possibly did. I don't think it will create any difficulty in the working out of this case.

Mr. Axelrad: We stipulated yesterday, orally, that there were leases made as these buildings were completed in 1945 for one year in all instances, which meant that they would expire in June, July, August and September of 1946.

We stipulated, secondly, that beginning about the middle of April 1946, if any leases were canceled, they did not make new leases.

The Court: Yes.

Mr. Axelrad: They changed their policy because of what the testimony showed. So that this [416] really is another way of getting at what we have already stipulated.

The Court: All right.

Mr. Chehock: I would like to make this statement to the Court, and that is in any situation, such as the one I pointed out, and the Court pointed out, where there appears to be an expiration date in 1947, I think the only fair assumption is that if it was vacated or canceled approximately a year before that, that there was another written lease of which we do not have any record.

The Court: Yes. All right. It will be received and marked as Exhibit III.

All right. You may proceed now.

Mr. Axelrad: Mrs. Woodruff.

Whereupon,

RUBY JEAN WOODRUFF

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your full name for the record, please?

The Witness: Ruby Jean Woodruff.

Direct Examination

Q. (By Mr. Axelrad): Mrs. Woodruff, were you ever employed by Artcraft Builders, Inc.? [417]

A. Yes, sir.

Q. When did that employment begin?

A. March 18, 1943.

Q. What were your duties?

A. Secretarial work.

Q. In the office?

A. Yes, in the office of Artcraft Builders.

Q. What was the corporation's activities, if you

(Testimony of Ruby Jean Woodruff.)

recall, at about the time you first became employed?

A. Residential construction.

Q. Do you recall whether they were attempting to buy land at that time? A. Yes, they were.

Q. What was the nature of that?

A. They were building tracts for sale at the time I went to work, and then they were buying land to build income property on for their own investment.

Q. For whose investment?

A. Mr. Pool and Mr. Murphy and their wives.

Q. Was that done? A. Yes, sir, it was.

Q. When this property was finished, was it leased? A. The rental property, you mean?

Q. Yes.

A. Yes, it was rented under leases. [418]

Q. Which tracts are you referring to now?

A. Tracts 11674 and 11451.

Q. That was the 22 apartments? A. Yes.

Q. And the 70 duplexes? A. Yes, sir.

Q. Who took care of the problems relating to rentals? A. Artcraft Builders.

Q. Did you keep the books of Artcraft Builders?

A. Yes, sir. I kept them after Mr. Clark died.

Q. When did he die?

A. He died in—I think it was March 1946. It was sometime in the early part of 1946. I kept all the records until that time. After he died, I kept the disbursements.

Q. Did you assist him while he was living?

A. Yes, sir.

Q. In keeping the books? A. Yes, sir.

(Testimony of Ruby Jean Woodruff.)

Q. How many people did Arteraft employ with reference to renting these various properties?

A. They employed about ten on maintenance work and lawn work and any work in connection with the rentals.

Q. What kind of people were they, what were their duties, specifically?

A. Well, in the case of the vacancies, [419] they cleaned the apartments, did any touching up work that had to be done inside. They took care of the lawns, any outside maintenance, anything that had to be done to the rentals.

Q. Did Arteraft supply utilities? A. Yes.

Q. Which ones?

A. The water was all that was paid.

Q. What about the trash collection?

A. The City picked up the trash and garbage.

Q. Who took the trash from wherever it was kept to the points of collection?

A. The tenants themselves put it in the service yard, and then our tract man put it outside the service yard to the alley where the City picked it up.

Q. How many people were engaged in these various activities? A. I think about ten.

Q. How many people were in the office?

A. Only myself after Mr. Clark died.

Q. What were your duties other than keeping records and books?

A. Well, to take care of the rentals and collection of rents and renting the property and drawing the leases.

(Testimony of Ruby Jean Woodruff.)

Q. You had a standard form lease, didn't you?

A. Yes, sir. [420]

Q. By drawing a lease you mean filling in the blanks? A. Yes.

The Court: When was it Mr. Clark died?

The Witness: I think it was early part of 1946. I am not positive of that.

Q. (By Mr. Axelrad): Was there much turnover in these apartments, people canceling leases for one reason or another?

A. Some months there were and some months there was none. We rented to Navy personnel and some months there would be quite a few transfers and then some months there wouldn't be any.

Q. Out of the 200 duplexes and the 100 buildings and the 140 units in the 70 duplexes and the 68 in the 22 apartments, you had a great number of tenants, did you not? A. Yes.

Q. At the peak, what would you think might be, in round figures, the number of leases that might be canceled or leases that might be expiring in a given month? A. Well,——

Q. Was it substantial or was it just small?

A. It was erratic. I don't think I could—some months it might run ten or 12. In another month, maybe it wouldn't run any.

Q. What was the arrangement between Edward Pool and [421] Associates and Artcraft with respect to taking care of these properties?

A. Artcraft was the rental agent for the properties.

(Testimony of Ruby Jean Woodruff.)

Q. How were the bills paid?

A. Artcraft paid the bills.

Q. What were the bills that they would have to pay in the course of an average month?

A. Well, it was the utility bills, the bills for anything that had to be bought in maintenance work, lawn work, painting, or supplies of any kind to be kept on hand by the maintenance men.

Q. Who paid your salary?

A. Artcraft Builders.

Q. Did you ever consider yourself an employee of Edward Pool and Associates? A. No, sir.

Q. How did Edward Pool and Associates pay for these amounts that Artcraft was paying on Edward Pool and Associates accounts?

A. They were charged on our books to the account of Edward Pool and Associates.

Q. Was that deducted when the net rentals were remitted? A. Yes, it was.

Q. How often were the Associates paid the rents that were collected? [422]

A. Once a month.

Q. Did you make out the checks?

A. I made out the checks after the auditors were done. After Mr. Clark died, Arthur Young & Company came down every month and made the audit. Then the checks were made out after that.

Q. Before Mr. Clark died, how was it done?

A. Mr. Clark did the figuring and then the checks were made out.

(Testimony of Ruby Jean Woodruff.)

Q. Did he make out one check or four checks, if you know, each month?

A. I believe there was one check. I am not positive. The books would reflect that.

Q. Now, were you ever present in the office when anyone came in to ask about buying? Did that ever occur?

A. Yes, quite a number of times.

Q. Under what circumstances?

A. We had tenants living in the properties that occasionally wanted to know if the properties were for sale, and they were interested in buying them.

Q. Would they ask you?

A. Yes. Sometimes they asked me and sometimes, if Mr. Pool or Mr. Murphy happened to be in the office, they would ask them. Usually it was me.

Q. What would they tell them, or what would you tell [423] them?

A. I would tell them I would ask, that I didn't think they were for sale, but I would ask Mr. Pool or Mr. Murphy.

Q. Did you ask? A. Yes, several times.

Q. What did they say?

A. They said they were holding them, they didn't want to sell them.

Q. Was this a fairly frequent occurrence?

A. Yes.

Q. Did you in each case ask Mr. Murphy and Mr. Pool?

A. Yes. I always told them any time anybody

(Testimony of Ruby Jean Woodruff.)

had inquired about a sale, I always told them, so if they had changed their minds, they could say so.

Q. After the Artcraft had finished its last buildings, which we have stipulated occurred in 1945, how much time generally would Mr. Murphy spend in the office? A. Not very much.

Q. Were there some days he didn't come down?

A. There were a number of days he didn't come down.

Q. Would there be days when he was in the city?

A. Yes.

Q. When he would come down, how often would he stay?

A. It would vary from maybe just a few minutes to see if there would be any calls or mail, and sometimes maybe a [424] couple of hours, if he had any letters to write or any calls to make.

Q. Were you present when Mr. Boland moved into the office? A. Yes, sir.

Q. Do you know what the relationship was between Mr. Boland and the Associates?

A. He was a broker selling the houses, the duplexes.

Q. Were you present most of the time when he was selling the houses?

A. Yes, sir. I was in the office every day.

Q. Did Mr. Pool or Mr. Murphy assist Mr. Boland in selling? A. No, sir.

Q. I didn't hear the answer. A. No, sir.

Q. They never did anything towards selling them? A. No, sir.

(Testimony of Ruby Jean Woodruff.)

Q. Were you ever present when Mr. Boland was talking to newspaper people about advertisements?

A. Yes.

Q. Or writing advertisements? A. Yes.

Q. What occurred then?

A. I know sometimes they would call on the phone to [425] see if he wanted to change his ad or if he wanted to keep running the same ad. That was mostly the Long Beach papers. A representative of the Los Angeles papers would come in sometimes and together they would work out an ad.

Q. Were you present in court yesterday when Mr. Boland was on the stand? A. Yes.

Q. There was an extended discussion about whose records were contained in these boxes, the escrow papers. A. Yes.

Q. Do you know anything about those records?

A. Yes, sir.

Mr. Chehock: What did she say?

(The answer was read.)

Q. (By Mr. Axelrad): What are those papers insofar as you know?

A. Some of those records were Mr. Boland's records that he had when he sold the places. Others were my records. When everything was sold and Mr. Boland left, I had given him a drawer in the file cabinet for his records, but I needed more space, so I took everything and consolidated and put them all in the same envelope so everything referring to it would be together.

(Testimony of Ruby Jean Woodruff.)

Q. You mean these envelopes contained part of the Artcraft records and part of Mr. Boland's?

A. Yes, sir.

Q. And you personally put them all together?

A. Yes, sir, I did.

The Court: I could have told you that yesterday.

Mr. Axelrad: I thought so, too, your Honor, but I wanted the record to show it.

Q. (By Mr. Axelrad): Did you type generally any letters that Mr. Murphy might write to anybody? A. Yes, sir.

Q. Were you his personal secretary?

A. Yes.

Q. Do you recall whether there were any letters written to Mr. Boland?

A. Yes, sir, there was.

Q. What was their nature?

A. There was a letter written to him with a reference to selling the 70 duplexes and giving him authority or the exclusive or whatever it is called, to sell the 70 duplexes.

Mr. Chehock: I am going to object unless the witness can premise this by stating that the letters are not available. If the letters are available, that is the best evidence.

The Witness: I don't know——

The Court: Wait a minute. Read the question to me. [427]

(The question was read.)

The Court: Did you have anything to do with writing the letter?

(Testimony of Ruby Jean Woodruff.)

The Witness: Yes. It was dictated to me and I wrote it, but I can't find a copy of it.

The Court: All right. Go ahead.

Q. (By Mr. Axelrad): Were you requested in the course of the preparation of this trial to bring all of the records relating to the activities that are in issue in this case to my office?

A. Yes, sir.

Q. Did you bring everything that you could find?

A. I brought everything I could find.

Q. Was there any discussion about selling the 100 houses at the time that the 70 were first put on sale? A. No, sir.

Q. You don't recall any conversations relating to that? A. No, sir.

Q. When the 100 were placed on sale, was that handled generally in the same manner by Mr. Boland? A. Yes, sir.

Q. Did Mr. Murphy or Mr. Pool have anything to do with that? A. No, sir.

Q. Were they frequently out of town during the general [428] period? A. Yes, they were.

Q. Did they sometimes come into the office?

A. Oh, yes.

Q. While these things were being sold?

A. Yes.

Q. What would they be doing there? What would they do?

A. They were never there for very long at a

(Testimony of Ruby Jean Woodruff.)

time. It was mostly to check the mail or to sign any escrow instructions, and calls.

Q. Do you recall the prin'.d form deeds that were used and are found in these escrow papers?

A. Yes, sir.

Q. Were those deeds, if you recall, signed in advance by Mr. Pool and Mr. Murphy and their wives? A. Yes, they were.

Q. Then what would happen to the deeds?

A. Well, part of them were signed with Mr. Pool's signature left off, part with Mr. Murphy's signature left off. Then I kept them locked in the safe. As they were needed, whichever one happened to come in first, then I got them out and had them sign them.

Q. During this general period when the 70 were being sold, and later the 100, was there any discussion, to your knowledge, of the 22 apartments being sold? [429] A. No, there was not.

Q. They were never mentioned?

A. Not to my knowledge.

Q. Do you know why they were not sold?

A. They were a much better investment, and they were always—well, they were their baby, so to speak, that they were going to keep.

Q. Do you know when those were sold?

Mr. Chehock: Just a minute. I move to strike that as hearsay testimony.

The Court: I think it is more of a conclusion.

Mr. Chehock: A conclusion.

(Testimony of Ruby Jean Woodruff.)

The Court: I will regard it as so, but I am going to let it stay in there.

Q. (By Mr. Axelrad): When were the 22 apartment buildings first offered for sale, to your knowledge? A. In the summer of 1949.

Q. Who sold those?

A. Mr. Smith. He was a real estate broker.

Q. Can you further identify him?

A. Marshal A. Smith.

Q. Do you know what arrangements there were about that? Was he paid a commission or a salary, or how did that work?

A. He was paid a straight five per cent commission. [430]

Q. What was the status of the tenancy in these 22 apartments at about that period?

A. We had quite a few vacancies.

Q. Why did you have vacancies?

A. It was getting harder to rent, people were getting more choosey, and we were limiting them to couples only, that's all there was room for.

Q. Was there a substantial vacancy?

A. Yes. At the time that they decided to put it on the market, I think we had 16 vacancies.

Q. Out of how many? A. Out of 68.

Q. Did that enter into any of the discussions about selling them?

A. Yes, sir, I think it did.

Q. Do you know whether it did?

A. Yes. I heard them talking about the number

(Testimony of Ruby Jean Woodruff.)

of vacancies was so much more than it had been in the past.

Q. After these 68 units in the 28 apartments were disposed of in 1949, and the stipulation will show in 1950, was there any other rental property that the Associates owned?

A. Nothing except the business buildings.

Q. What business buildings?

A. The business buildings, one on the southwest corner [431] of Stearns and Lakewood, and one——

Q. Is that the one referred to as the Market Building?

A. Yes, it is. And the one on the southeast corner referred to as the bank building.

Q. When was the market building sold?

A. It wasn't sold.

Q. They still own it? A. Yes, sir.

Q. Do they still rent it? A. Yes, sir.

Mr. Chehock: Who is "they"?

The Witness: Mr. Pool and Mr. Murphy and their wives.

Q. (By Mr. Axelrad): What about the bank building? A. It is sold.

Q. Were you present yesterday when Respondent's counsel showed various exhibits to Mr. Boland relating to August escrow instructions on the 100 duplexes? A. Yes, sir.

Q. And he asked him and other witnesses why there was typed on a carbon copy in apparently

(Testimony of Ruby Jean Woodruff.)

original typing some legend relating to the signing date? A. Yes.

The Court: Why don't you show her one? [432]

Mr. Chehock: VV or WW.

Q. (By Mr. Axelrad): I hand you Respondent's Exhibit WW, the third paper in this exhibit labeled Escrow Instructions, Bank of America—Is that correct? A. Yes, sir.

Q. Would you say that this is a carbon or an original? A. That is a carbon.

Q. Now, will you read what is typed in below the line "By"? A. Signing date 9-23-46.

Q. Would you say that that was a carbon or typed on originally?

A. No, it looks like original.

Q. It was brought out yesterday in testimony that this appeared on many escrows that were apparently opened in August.

The Court: In 1946?

Mr. Axelrad: Yes, in 1946.

Q. (By Mr. Axelrad): And the record apparently shows it didn't occur on any escrow instructions that were relating to sales occurring in later months. A. Yes, sir.

Q. Do you have any explanation for this language and [433] why it appeared in the August escrows and apparently not in the other ones?

A. Yes.

Q. What is that explanation?

The Court: Did you have anything to do with it?

(Testimony of Ruby Jean Woodruff.)

The Witness: I didn't type it on there, but I know why it was typed on.

The Court: Did you have anything to do with the typing on of it?

The Witness: No, sir.

The Court: Or directing it to be typed?

The Witness: No, sir, I didn't have anything to do with the typing of it, but I know the circumstances under which it was typed on.

The Court: You may proceed.

Mr. Axelrad: I didn't know your Honor was through. Pardon me.

The Court: Proceed.

Q. (By Mr. Axelrad): Let me rephrase the question. What was the normal procedure relating to the escrow instructions, if you know? Where were they prepared?

A. They were prepared by the escrow department and then an original and one copy came out to the office, the original to be signed and sent back, and the copy was [434] supposed to be retained in our office. That was our office copy. On these that that date is marked on, it is there due to the difficulty in financing. When they were finally signed, when the financing was arranged and they were signed, I sent them back to the bank, but I forgot to pull the copies and keep them for our files.

The Court: Copies of what?

The Witness: The copies of the escrow instructions that they had sent out the original and a copy on each one.

(Testimony of Ruby Jean Woodruff.)

The Court: Is that what you are talking about when you say "when they were signed"?

The Witness: When the original was signed.

The Court: The original of what?

The Witness: Of the escrow instructions.

The Court: Yes.

The Witness: Instead of my pulling the copy of each one and keeping it for our files, I carelessly sent both the original and the copy back to the bank, to the escrow department. They took the copies and put the date that they were signed on there, typed it on there, and sent it back out to me for my files.

The Court: Really all you know is that that date was on there when it came back?

The Witness: That's all I know, is the date was on there when it came back. [435]

The Court: That is when the copy came back?

The Witness: When the copy came back, yes, sir.

The Court: You weren't over at the bank?

The Witness: No, sir.

The Court: All right.

Q. (By Mr. Axelrad): After the later escrows, do you recall any other instance when you forgot to hold the copy and sent it back to the bank?

A. I don't think there is any other, because I separated them when they came in after that, filed our copy, and then had the original signed and sent back.

Q. Was it customary to accumulate a great num-

(Testimony of Ruby Jean Woodruff.)

ber of escrow instructions, or send them back currently as they were executed?

A. As a general rule, if Mr. Pool or Mr. Murphy were there to sign them, I sent them right back. If they weren't there, why, I held them until one or the other was there, and then sent them all back.

Q. These August escrows, were they retained for a period, or do you recall?

A. You mean these instructions?

Q. Yes, the escrow instructions.

A. They were kept until the financing was arranged. There was no point in signing them and sending them back [436] unless the financing was arranged on them.

Mr. Axelrad: I have no other questions, your Honor.

Cross Examination

Q. (By Mr. Chehock): Mrs. Woodruff, on that matter on which you have just been interrogated with regard to the date that appears below on the copy in the escrow instructions, which is found in Exhibit WW, when you say that that date appears there, do I understand from your testimony that that original escrow agreement was signed in your presence and then mailed to the Bank of America?

A. They were signed in the office, not always in my presence. They didn't have to be notarized. But they were signed and put back on my desk.

Q. And then they were——

A. Then I mailed them back to the escrow department.

(Testimony of Ruby Jean Woodruff.)

Q. Then they came back to you, and when they came back to you, they had this date on here?

A. Yes, sir.

Q. The date, then, has reference, not to the signing of the escrow, but rather the date of the signing of the deed, is that correct?

A. I don't know. I can't say what it has reference to. It was on there when they were sent back to me. I presumed that it was the date that was on the original. [437]

Q. Of the deed?

A. That is just presuming.

Q. Of the deed?

A. No, of the escrow instructions.

The Court: Rather obviously it wasn't that. But the record shows what it is, Mr. Chehock.

Mr. Chehock: All right.

Q. (By Mr. Chehock): I refer you now to Exhibit 24. I note you took the acknowledgment on this deed of the 100 duplexes from Artcraft to the four individuals. A. Yes, sir.

Q. Do you keep a record of the notarial acknowledgments that you take? A. Yes, sir.

Q. Do you have that record here?

A. Not here in the court room.

Q. Do you know whether or not you took this acknowledgment on March 21, 1946? A. Yes.

Q. Did you also notarize or do you know anything about this deed that some testimony has been given here on, a lost deed made earlier?

A. Yes, sir.

(Testimony of Ruby Jean Woodruff.)

Q. Did you notarize that deed? [438]

A. No, sir, I didn't. That was notarized in Mr. Swaffield's office. I mean it was drawn up and taken care of in Mr. Swaffield's office.

Q. So you wouldn't have any knowledge of that?

A. No, sir, except that I know the conversation was that the deed was lost.

Q. Do you recall the recording of that deed in Exhibit 24? Did you handle the recording of the deed?

A. I don't remember whether I mailed that in for recording or not.

Q. Do you recall approximately how much time elapsed after you notarized it before it was recorded? A. No.

Q. Mrs. Woodruff, you kept the books for Edward Pool and Associates, did you not?

A. Yes, what little there was.

Q. You were employed by them to that extent, weren't you?

A. No, sir. Arteraft was supposed to keep what records there was for Edward Pool and Associates.

Q. For whom?

A. For Edward Pool and Associates.

Q. But you did keep the records of Arteraft and you did keep the records of Edward Pool and Associates, is that right? [439] A. Yes.

Q. Do you have any personal knowledge of the printing of these grant deeds for the 70 duplexes tract and the 100?

A. No. It wasn't done by Artcraft.

(Testimony of Ruby Jean Woodruff.)

Q. Do you know what I have reference to?

A. You said the deeds for the 70 and for the 100, the grant deeds.

Q. You know what I have reference to, don't you? A. Yes, sir.

The Court: Here is a copy of one of them in this Exhibit WW.

The Witness: Yes, sir.

The Court: That is what you have reference to?

The Witness: Yes, sir.

Q. (By Mr. Chehock): Do you know when they were printed? A. No.

Q. Do you know how many vacancies there were, approximately, in the 70 and the 100 duplexes at the time of sale?

A. I think there were only two in the 70, and in the 100, I don't know exactly how many, but there wasn't very many at the time they were put on the market.

Q. Doesn't Artcraft handle the rental for Edward Pool and Associates of the market building?

A. No, sir. [449]

Q. They have, haven't they? A. No, sir.

Q. Artcraft has never been rental agent for Edward Pool and Associates? A. Yes, sir.

Q. For the property of the market building?

A. Yes, sir.

Q. Now, wait a minute, Mrs. Woodruff.

A. Not on the market building, no, sir.

The Court: When was the market building constructed, if you know?

(Testimony of Ruby Jean Woodruff.)

The Witness: It was finished in October 1944.

The Court: Go ahead.

Q. (By Mr. Chehock): And Arteraft has never been rental agent of Edward Pool and Associates for that building?

A. No, not for the market building.

The Court: Did you keep the books and records with respect to that?

The Witness: Yes. That went straight in the Associates.

The Court: But you kept the books and records?

The Witness: Yes.

Q. (By Mr. Chehock): You have given some testimony—— [441]

The Court: You didn't draw any pay for that, is that the idea?

The Witness: No.

Mr. Chehock: Are you through?

The Court: Yes. Well, I would ask one more question.

By that you mean you didn't get any money that was given to you as coming directly from Pool and Murphy?

The Witness: No, sir.

The Court: Or their wives.

The Witness: No, sir.

The Court: All right. Go ahead.

Q. (By Mr. Chehock): Was there a separate bank account for the market building, or did the rentals for that go in with the rest of them?

A. The rental moneys went into Arteraft Build-

(Testimony of Ruby Jean Woodruff.)

ers, and then Artcraft, at the end of the month, or whenever an audit was made, paid it over to the Associates, and that went into the Associates' account.

The Court: That included the market building rentals as well as the other?

The Witness: The market building rentals went directly into the Associates' account. [442]

Q. (By Mr. Chehock): And not through Artcraft? A. No, sir.

Q. I think you gave some testimony regarding in August of 1946 that it took some time there to arrange the financing. What did you have in mind?

A. I don't know very much about it except the Bank of America had financed the 70 duplexes, and it was thought that they would finance the 100, and then something went wrong with it, they didn't take them, and I know other financing had to be arranged on them.

Q. What other financing was arranged?

A. Well, they finally went through Insurance Funds Mortgage Company. I don't know any of the details. I was not familiar with that. But I know that they were handled through Insurance Funds Mortgage Company.

Q. Who handled that? Who made those arrangements on the financing?

A. Mr. Boland and Mr. Murphy.

Q. Do you know with whom they made the arrangements? A. No.

(Testimony of Ruby Jean Woodruff.)

Q. Did you do any of the secretarial work on that end of it?

A. I don't think there was any letters written. I don't remember any. [443]

Q. Who are the folks that finally financed the purchasers on these 100 duplexes?

A. The Insurance Funds Mortgage Company. I don't know who they represent, but that is the name of the company.

Q. With whom did you folks deal? Did they have an office in Long Beach?

A. In Los Angeles.

Q. In Los Angeles? A. Yes.

Q. You dealt with the folks here in Los Angeles on that? A. Yes, sir.

Q. All leases on the 70 and on the 100 duplexes were made with the tenants with the Arteraft signing the leases as landlord of the property, is that right? A. Yes, sir.

Q. And that was true even of the last leases they made, what leases they made on the 70 and the 100?

A. Yes, and on the 22, on all of them.

Q. Who bought the 70 and the 100 duplexes? Mostly veterans or nonveterans?

A. Veterans. On the 100, it was, I think, almost all, if not all bought by two veterans.

Q. And the 70?

A. On the 70, I believe it was mostly veterans, but it was one veteran. [444]

The Court: What do you mean by "veterans"?

The Witness: That is on the GI loans.

(Testimony of Ruby Jean Woodruff.)

The Court: Men who had formerly been in the Armed Services?

The Witness: Yes, sir.

The Court: And were out, is that what you mean?

The Witness: Yes, sir, and discharged.

The Court: All right.

Q. (By Mr. Chehock): Well now, the 70 duplexes you say were sold mostly to nonveterans, or some to both? A. No, mostly to veterans.

Q. Of the 70? A. Of the 70.

Q. But they were sold to mostly one veteran rather than to two veterans, is that it?

A. I don't believe there was any duplex in the 70 that was sold to two veterans.

Q. Where the particular duplex was in the possession of the tenants and not vacant when sold—were there situations like that? A. Yes.

Q. In the 70 and the 100? A. Yes.

Q. What was the procedure in getting occupation for [445] the buyers? I mean, how did the buyers get possession of the particular duplex that they had purchased?

A. I don't know that. I didn't have anything to do with them after they were sold.

Q. Now, most of these buyers were occupant buyers, weren't they? They were buyers that wanted possession? A. Yes.

Q. You must have known something about that.

A. If there was a vacancy occurring in it during the time that the place was for sale, it was left va-

(Testimony of Ruby Jean Woodruff.)

cant for the convenience of the new buyer, but otherwise they went through their regular channels, I guess, and got possession of one side after they bought it.

Q. These folks weren't buying unless they knew they were going to get possession, is that right?

A. I don't know. I didn't talk to them.

Q. I am sure that they must have been concerned about whether they were going to get possession. Didn't you hear any talk about that at the time of the sales? A. Sometimes.

Q. How long did it take these purchasers to get possession where there was no written lease?

A. I don't know just how long it took.

Q. Well, about how long?

A. I think—I don't know, I think it took about three [446] months, but I don't know for sure.

Q. Do you know what steps they took to get possession?

A. I believe they had to go through the OPA.

Q. Where they had written leases for a longer period, then of course they had to wait for the period to expire, is that right? A. Yes.

Q. How many available units for rent are there in the market building?

A. There isn't any.

Q. How many units are there in the market building that are rented? A. Three.

Q To whom were the checks made out for the rent? A. To Edward Pool and Associates.

Q. To Edward Pool and Associates?

(Testimony of Ruby Jean Woodruff.)

A. Yes.

Mr. Axelrad: Your Honor, I would like to make an observation at this point. It is not truly material to Petitioners' case, as I view it, but I don't know the procedure in this sort of situation. It was stipulated, and I refer to page 7 of the stipulation, paragraph 4:

"Artcraft performed the services of rental agent for Associates for the period Associates owned the aforesaid properties." [447]

That refers in context to the 22 apartment buildings and the 70 duplexes, and then it goes on:

"Together with 100 duplexes and a market building, both referred to hereinafter."

So that the testimony that Mr. Chehock is eliciting is contrary to the stipulation and there must be some confusion at some point, but I thought I ought to call the Court's attention to the fact.

The Court: The record will show the statement of counsel.

Mr. Chehock: I will say this testimony is a surprise to me. I thought it was as we had stipulated. However, I don't think it is too material.

The Court: We sometimes have instances where that has happened. If you will go back into the books at about 1935, you will find the case where the opinion was written by McMahon where we had some problem that we had to deal with where there was a discrepancy between the stipulation and other evidence, and in that instance it developed that it was material.

(Testimony of Ruby Jean Woodruff.)

Mr. Chehock: That's all.

Mr. Axelrad: I would like to ask a few questions.

Redirect Examination

Q. (By Mr. Axelrad): You say that the checks on the market building [448] were paid directly by the tenants, is that correct, to Edward Pool and Associates? A. Yes.

Q. How did they send the checks? By mail or personally?

A. Well, one mailed them in, and the other one brought them in. The market always mailed theirs in.

The Court: Mailed it where?

The Witness: Mailed them to the office.

Q. (By Mr. Axelrad): To Artcraft's office?

A. To Artcraft's office.

Q. But addressed to whom?

A. Edward Pool and Associates.

Q. What was the situation with respect to the apartments and duplexes? How did you get the money?

A. They paid it to me in the office.

Q. In cash?

A. Sometimes checks, sometimes cash. If it was a check, it was made out to Artcraft Builders.

Q. Did they bring them in?

A. Most of them brought them in.

Q. The leases on the 70 duplexes and 100 duplexes and 22 apartments, when there were leases, were between the tenants and whom?

(Testimony of Ruby Jean Woodruff.)

A. Artcraft Builders. [449]

Q. Do you know who the lease was between on the market building?

A. That was between Edward and Lottie Pool, Edna Murphy and William K. Murphy, and the lessee.

The Court: Right at that point, you put one of those leases in the record?

Mr. Axelrad: Yes, that's right, your Honor.

The Court: Let me see that.

Mr. Axelrad: It is Exhibit G-7.

The Court: All right. You may proceed.

Q. (By Mr. Axelrad): This difference that you have testified to concerning the way the leases ran, did that have anything to do with your answer about rental agent? A. No.

Q. What was your answer based on when you said that Artcraft did not act as rental agent for the Associates with respect to the market building?

A. They handled the rentals on the residential income.

Q. Who did any repairs that were necessary on the market building, if there were any?

A. Well, there weren't any.

Q. No repairs were ever made?

A. No repairs were made until recently, and they handled that themselves. [450]

Q. Who paid the taxes?

A. Edward Pool and Associates with their own check.

Q. Who would write the check for them?

(Testimony of Ruby Jean Woodruff.)

A. I did.

Q. And you kept the books for them on the market building, as well as everything else?

A. That went into the Associates' books.

Q. Is it a correct statement you did everything with respect to the market building that you did with respect to the duplexes? A. Yes, sir.

Q. Was there some written agreement about Artcraft serving as rental agent which said that they were rental agent for the apartments and not for the market building? A. No.

Q. What is your conclusion based on that they were not, then? A. What do you mean?

The Court: I wouldn't know how to understand that question and I think it is necessary that I do. Let's go back and read the record. Read two or three questions and answers back.

(The record was read.)

The Court: "That they were not, then." What do you mean by that? [451]

Mr. Axelrad: Could we strike the last question and I will rephrase it?

The Court: All right.

Q. (By Mr. Axelrad): What is your conclusion based on that Artcraft was not rental agent for Edward Pool and Associates with respect to the market building?

The Court: Well, what are you talking about? What sort of conclusion? Legal or factual conclusion?

Q. (By Mr. Axelrad): You answered that Art-

(Testimony of Ruby Jean Woodruff.)

craft was not rental agent for the Associates relating to the market building. A. Yes.

The Court: What were the facts?

Q. (By Mr. Axelrad): What were the facts?

The Court: As you knew them.

The Witness: The tenants mailed in the checks made out to Edward Pool and Associates.

Q. (By Mr. Axelrad): Is that the only fact?

A. That is the only fact.

Mr. Axelrad: That's all.

Mr. Chehock: I would like to ask one other question.

The Court: All right. [452]

Recross Examination

Q. (By Mr. Chehock): I refer you, Mrs. Woodruff, to Respondent's Exhibit HHH, and ask you if these are the cards that appear in the files for the 100 duplexes? I think you know what they are.

A. Yes.

Q. On some of these are written in pencil, others written in ink, and some are written typed out, I mean, "No Lease," many of them contain "No Lease," such as this. Is that your handwriting?

A. Yes, sir.

Q. Were you the one that made all these records on these cards? A. Yes.

The Court: She very obviously didn't, Mr. Chehock, because some that were shown to Boland, he stated the "No Lease" was printed on in ink and it was printed on in exactly the same stroke of the

(Testimony of Ruby Jean Woodruff.)

printing in ink that Boland himself testified was his own printing, so it varied. The writing, from observation, was not likely to have all been made by the same person. I think the same thing is rather obvious as was obvious yesterday, that this witness possibly did some of them, he possibly did some of them, and then someone did the notation in typing. I don't think it makes any difference, though. [453]

Mr. Chehock: I don't think it does either. I was generalizing because we haven't got them all.

The Court: I think it is just as well, since the point was made about this particular notation, which was one of the very few that were in pencil, to know that is her handwriting. I think it might also be helpful, if any point is to be made of it, as to her knowledge of the circumstances under which those entries would be made on those cards, whether she made them in handwriting or whether Mr. Boland made them, or whether she or someone else typed them on there, if she has any knowledge of the circumstances, I think that might be something we could find out.

Mr. Chehock: I was about to ask that.

The Court: All right. You go ahead then.

The Witness: I gave the information. Whether I wrote it on there or not, I gave the information from my card in the Kardex file.

The Court: What would be the system when they would get that information? Would Mr. Boland ask you?

(Testimony of Ruby Jean Woodruff.)

The Witness: Sometimes he would hand me a card. Sometimes his secretary would ask me and she would write it on. Sometimes he would ask me and he would write it on. But the information came from information that was off the files in the Kardex file. [454]

Q. (By Mr. Chehock): From whose cards, do you mean?

A. From my cards. It was a Kardex file where I recorded the rent payments. It was a regular Kardex system.

Q. That notation, for instance, on this HHH, where it says, "No Lease," opposite 2220 Grand Avenue, does that mean there was no lease in existence on that particular unit or duplex?

A. Yes.

Q. Does it mean no lease as of what time?

A. Well, that I couldn't tell you. As of the time when the cards were compiled, and that was after he started selling the duplexes.

The Court: That would be, wouldn't it, during the period that Mr. Boland was using the cards in the course of his work in making the sales?

The Witness: Yes, it would be.

Mr. Chehock: That's all.

The Court: Do you have any further questions?

Mr. Axelrad: I would like to ask one question that probably doesn't belong at this point, but I left it out in my original examination.

The Court: All right. Go ahead. [455]

(Testimony of Ruby Jean Woodruff.)

Redirect Examination

Q. (By Mr. Axelrad): Did you ever have a contact, or did anyone contact Arteraft Builders, Inc., to your knowledge, from Caldwell Banker, the real estate people? A. Caldwell Banker?

Q. Yes. Isn't that the name?

The Witness: I think it is Colwell, C-o-l-w-e-l-l.

Q. What is the rest of the name?

A. Banker Company.

Q. Banker?

A. I believe so, yes, sir. I don't know whether there is an "s" on that Banker or not.

Q. What was your contact with them, if any?

A. They came into the office.

Q. When?

A. One of their representatives did. I believe it was in the early part of 1949. It was sometime before summer. It must have been in the spring of 1949. They thought that they had somebody that was interested in buying the tract 11674 as a whole.

The Court: Which one is that?

The Witness: That is the 68 rentals, 22 buildings containing 68 apartments.

The Court: All right. [456]

Q. (By Mr. Axelrad): This was in the spring of 1949? A. I believe it was.

Q. Did you ask them to come in or did Mr. Murphy, to your knowledge?

A. No, not to my knowledge.

Q. They came in and they said they had a buyer? A. Yes.

(Testimony of Ruby Jean Woodruff.)

Q. And what transpired then?

A. Well, they wanted an exclusive on the tract.

Q. Then what occurred?

A. I think they were given a 90-day exclusive, but nothing ever came from it.

Q. They did not sell it? A. No, sir.

Q. Did they attempt to sell it, do you know?

A. I don't know that.

Q. You don't know? A. No.

Q. Was this property ever listed with any other broker? A. No, sir.

Q. Was the 100 duplexes tract ever listed with any other broker other than Mr. Boland?

A. No, sir.

Q. Was the 70? [457] A. No, sir.

Q. Was the market building? A. No, sir.

Q. Was the bank building?

A. Not to my knowledge.

Q. The bank building?

A. The bank building was sold by a broker, but whether he had a listing on it or not, I don't know.

Q. Do you know anything of the circumstances under which the bank building was put on the market? A. No, sir, I don't.

Q. You don't know why it was sold?

A. No.

Mr. Axelrad: That's all.

Mr. Chehock: I would like to state to the Court in view of the witness' testimony with respect to the rental on the market, I think her statement is probably more correct than the stipulation which

(Testimony of Ruby Jean Woodruff.)

Petitioners' counsel has called to your attention, and I am calling to your attention, in the event it is necessary to take that into account that fact, since the written stipulation and the testimony is at variance.

The Court: The record will show the statement of counsel.

Mr. Axelrad: Your Honor, it is my own feeling [458] there isn't any conflict. Her explanation was involved and I think it is quite immaterial, in any event.

The Court: Any questions further from this witness?

Mr. Chehock: No.

The Court: I have a question or two.

You were asked by counsel for the respondent on cross examination about your work as notary in taking the acknowledgment of a deed.

The Witness: Yes, sir.

The Court: That was a deed from Arteraft to individuals?

The Witness: Yes, sir.

The Court: You have testified about these deeds to the purchasers when these various duplexes were sold. Those were in the form of grants by Edward Pool, Lottie Pool, Edna Murphy and William K. Murphy as individuals?

The Witness: Yes, sir.

The Court: Did you take the acknowledgments?

The Witness: Yes, sir.

The Court: Their acknowledgments on those?

(Testimony of Ruby Jean Woodruff.)

The Witness: Yes, sir.

The Court: What did you do? Well, on what dates were those acknowledgments taken?

The Witness: They were signed—in the beginning they were all signed in front of me, Mr. and Mrs. Pool and [459] Mr. and Mrs. Murphy, they were signed in front of me in the office. Then I put them in the safe.

The Court: Yes.

The Witness: Then when they were ready to be acknowledged, well, I had seen the signature and seen them signed.

The Court: Well, you mean they weren't there when the grant was made, that is, when a purchaser was found?

The Witness: One or the other of them were there and they had to be completed and another signature put there.

The Court: Yes. What transpired then?

The Witness: They were in town at the time and they knew that that deed was made up.

The Court: Yes. Did you do anything about their acknowledgment other than with respect to the one that came in later and signed?

The Witness: I don't understand what you mean.

The Court: Well, as I understand it, three of them would sign a blank deed.

The Witness: Yes, sir.

The Court: There was rather obviously no grant there.

(Testimony of Ruby Jean Woodruff.)

The Witness: No.

The Court: Because there was no one to grant anything to [492]

The Witness: No.

The Court: Did you see them or speak to them, or anything, afterwards about when a deed was to be made, when you did have a purchaser and there was a grant to be made, those who had already signed, or did you just take the blank sheet out with their signatures on it and fill it in?

The Witness: I took it out with their signatures on it and filled it in. Then somebody, one or the other of the form, had to know about it.

The Court: What do you mean?

The Witness: Because it had to be signed.

The Court: There was one signature yet to be signed?

The Witness: Yes, sir.

The Court: And what did you do?

The Witness: Then I acknowledged it.

The Court: Did you put different dates on it? Did you call them up about it, or just go through the formality?

The Witness: No. I just acknowledge it as of the day it was completed.

The Court: The deeds, then, would show under your seal and signature acknowledgment of all of them on a given date, on one date, is that right?

The Witness: On the date that it was complete.

The Court: All right.

Mr. Axelrad: May I ask a question?

(Testimony of Ruby Jean Woodruff.)

The Court: I will allow you to ask your questions. I always give counsel for both parties the opportunity of asking questions after I have finished, because my questioning may suggest something that they think needs clarifying.

Now, turning back to your functions with respect to rents and so forth on the duplexes and on the market buildings, where rents on the duplexes were paid in by check, to whom would those checks normally be drawn?

The Witness: You mean on the duplexes and apartments?

The Court: Yes.

The Witness: Artcraft Buildera.

The Court: What about the market building, the tenants there?

The Witness: They made out their checks to Edward Pool and Associates.

The Court: Would your receive those checks?

The Witness: Yes, sir.

The Court: How would they come to you? By mail or in personal delivery?

The Witness: They were mailed to the office.

The Court: Through the mail?

The Witness: Well, on the market, it came through [463] the mail, and on the drug store it came to the office.

The Court: Artcraft had a bank account, did it?

The Witness: Yes, sir.

The Court: Was there a bank account in the name of—what is the term? Associates?

(Testimony of Ruby Jean Woodruff.)

The Witness: Edward Pool and Associates.

The Court: Yes.

The Witness: Yes.

The Court: Was there a bank account in that name?

The Witness: Yes, sir.

The Court: Who kept the check book and so forth on those accounts?

The Witness: I did.

The Court: You did?

The Witness: Yes, sir.

The Court: Did you make the deposits in those accounts?

The Witness: Yes, sir.

The Court: When a check would come in for rent on the market building from a tenant in the market building, would that be made out to Edward Pool and Associates?

The Witness: Yes, sir.

The Court: Is that the usual way?

The Witness: Yes, sir.

The Court: Did you endorse it and deposit it in that [463] account?

The Witness: Yes, sir.

The Court: Is that what happened?

The Witness: Yes, sir.

The Court: What about these distributions that were made monthly, I believe you said, by Artcraft to these individuals? Would those checks be made out to Edward Pool and Associates?

The Witness: I think there was, I am not posi-

(Testimony of Ruby Jean Woodruff.)

tive, the books would reflect, but I think there was one check made out to Edward Pool and Associates and deposited in Edward Pool and Associates' account.

The Court: You wouldn't then, normally and as a general rule, you didn't have those checks for deposit in this bank account, Edward Pool and Associates, that you kept?

The Witness: You mean the checks from Artcraft to Edward Pool and Associates?

The Court: I mean the checks from Arteraft which distributed what was left over of the rents on the duplexes.

The Witness: Yes.

The Court: As I understood, you said that each month the balance was distributed by checks?

The Witness: Yes, sir.

The Court: Made out monthly?

The Witness: Yes, sir. [464]

The Court: What I am trying to find out is how those checks were made out, to whom they were made out, and whether or not they were handed to someone else or whether you deposited them in some bank account or bank accounts yourself.

The Witness: No. I deposited them.

The Court: Where did you deposit them?

The Witness: In the Associates', in Edward Pool and Associates' bank account.

The Court: You typed out the checks and wrote out the checks that were drawn on that?

The Witness: Yes.

(Testimony of Ruby Jean Woodruff.)

The Court: Did you have any power to sign on that?

The Witness: No, sir.

The Court: You did not sign?

The Witness: No, sir.

The Court: I believe that is all. Do you have any questions?

Mr. Axelrad: Just one or two questions, your Honor.

Q. (By Mr. Axelrad): Did Artcraft or Edward Pool and Associates have an attorney during this period in the sale of the 70 or 100 duplexes?

A. Yes, sir.

Q. Who was he? [465]

A. Mr. Phil Swaffield.

Q. Was he a regular attorney? Was he on a retainer? A. He was on a retainer, yes, sir.

Q. Did he have anything to do with the drawing of the deeds that were used in all of these escrows? Do you know whether he did?

A. I think Mr. Boland talked to him, and he either helped draw up the deeds or he did draft the deeds, or something.

The Court: By that, do you mean this that later was printed in that form?

The Witness: Yes, sir.

Q. (By Mr. Axelrad): Do you know how the procedure got started of signing the deeds in blank?

A. Because they were gone so much, and Mr. Swaffield said it would be all right if they signed them in this way, like this one is signed, and I kept

(Testimony of Ruby Jean Woodruff.)

them in the safe and used them as we needed them, and either Mr. Boland's secretary filled them in or on a few I filled them in after she left.

Q. Would you put your notary stamp on when the three signed? A. No, sir.

Q. Did you when the fourth one signed? [466]

A. Yes, sir.

Q. And what date did your notarization bear?

A. The date of the last signature.

Q. When you actually notarized it?

A. Yes, sir.

Q. If you know, how do the individual associates get their money out of this Associates' bank account you have testified about?

A. They gave checks on it. It was distributed in four checks, one made out to each one of them to take it out of the Associates' account.

Q. You mean they would each write a check for one-fourth of the money that was in there?

A. I would write the check to each of the four for the same amount.

Q. On what bank account?

A. On the Edward Pool and Associates bank account.

Q. Does that mean that that bank account was kept with no balance all the time?

A. No. They left so much a month that accumulated in there for taxes and insurance and things that came due at the end of the year.

Q. What periods did you make out individual checks to them?

(Testimony of Ruby Jean Woodruff.)

A. I made them out every month, at the end of the [467] month.

Q. When you made those checks out, what did you do with the checks?

A. I gave Mr. Pool one after they were signed.

Q. You mean personally?

A. Yes, sir, and Mr. Murphy one.

Q. You handed it to them?

A. I handed it to them. I wrote a letter with Mrs. Pool's and with Mrs. Murphy's, and signed the letter, told what it was for, and mailed it out to their residences to them.

Q. That was done regularly?

A. There are copies of the letters, I think, in the files.

Q. You did that regularly?

A. I did that regularly, and they were signed by me.

Q. The letters were signed?

A. The letters were signed.

Q. Who signed the checks?

A. Mr. Pool or Mr. Murphy.

Q. Depending on who was there?

A. Depending on who was there, whichever one was there.

Mr. Axelrad: That's all, your Honor.

The Court: Any questions by the Respondent?

Recross Examination

Q. (By Mr. Chehock): Did you keep a record each time you notarized a grant deed?

(Testimony of Ruby Jean Woodruff.)

A. Yes, sir.

Mr. Chehock: That's all.

The Court: You are excused, if there are no further questions.

Mr. Axelrad: No further questions.

The Court: You are excused.

(Witness excused.)

The Court: We will take an intermission.

(Short recess taken.)

The Court: You may proceed.

Mr. Axelrad: Edward Pool.

Whereupon,

EDWARD POOL

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your full name for the record?

The Witness: Edward Pool. [469]

Direct Examination

Q. (By Mr. Axelrad): Are you the Edward Pool that is the Petitioner in No. 36108 and 36109?

A. Yes.

Q. What has been your profession or occupation during most of your life, Mr. Pool? A. Builder.

Q. Where did you first start building?

A. In Cincinnati, Ohio.

Q. How did you carry on your work? As an employee for someone?

(Testimony of Edward Pool.)

A. No. I have been a builder for myself all my life.

Q. What were you building?

A. Residential properties.

Q. How were they disposed of when they were built?

A. Well, usually called in a broker to sell them.

Q. When did you come to California?

A. Oh, about 18 years ago, I think.

Q. Are you a licensed contractor?

A. Yes, sir.

Q. Are you a licensed broker? A. No, sir.

Q. Licensed in any other state? A. No, sir.

Q. Has your wife ever been active in your business? A. No.

Q. Never worked while you have been married?

A. No, sir.

Q. How long have you been married?

A. 43 years.

Q. Were you one of the original stockholders of Arteraft Builders, Inc.? A. Yes, sir.

Q. What was Arteraft Builders' line of work after it was first organized?

A. Residential construction, contracting.

Q. When it built houses, how did it sell them?

A. Through brokers.

Q. Did you ever participate in selling anything that Arteraft built in the early days of its existence?

A. No, sir.

Q. What was your principal work for Arteraft? What did you do?

(Testimony of Edward Frook)

A. I had the building end of the company.

Q. Can you elaborate a little more on that?

A. I had nothing to do with the office. In other words, I did all the construction work and anything pertaining to the construction.

Q. Would you solicit bids? [471]

A. Yes, with subcontractors, yes.

Q. Work out plans? A. That's right.

Q. See that it got put together correctly?

A. Yes.

Q. Do you recall when you and Mr. Murphy bought the stock of Mr. Smith and Mr. Cook?

A. Yes.

Q. Approximately when was that?

A. I think around 1942 or 1943, along in there.

Q. Do you remember why you bought the stock, what occasioned it, if anything?

A. I had been wanting to build some income property, see, and they didn't want to go into anything pertaining to rental properties.

The Court: Who?

The Witness: Mr. Smith and Mr. Cook.

Q. (By Mr. Axelrad): What do you mean by you wanted to build rental properties? For what purpose? A. As an investment, you know.

Q. It wasn't your thought to build them for sale?

A. Oh, no, not income. You never build income for sale.

Q. Wouldn't it be possible to build apartments

(Testimony of Edward Pool.)

or [472] duplexes and offer them to other investors for sale?

A. It would be possible, yes, but it is pretty hard selling.

Q. That was not your idea, in any event?

A. No.

Q. Why did you want to do this?

A. At my age, I was trying to get an anchor out some place. I have been in this business so long, I know how hazardous it is. It is up and down. I wanted to get something permanent, with a permanent income, and I was the one that started the income idea.

Q. You mean Arteraft finally decided to build these as a result of your suggestions?

A. That's right.

Q. And requests? A. Yes.

Q. Was Mr. Murphy agreeable to this?

A. Yes, he was agreeable to it.

Q. After these houses, the first group of 22 apartments and 70 duplexes were built, were they ever placed on the market, to your knowledge?

A. No, sir. They would never have been put on the market, as far as I am concerned.

Q. That is before they were ultimately sold?

A. That's right. [473]

Q. Were you ever asked to sell them?

A. Yes, sir, lots of times.

Q. Who would ask you, under what circumstances?

(Testimony of Edward Pool.)

A. Various brokers trying to drum up business, that's all.

Q. Did any individual ever ask you to buy those?

A. Lots of times.

Q. Who?

A. Various people would come in the office, just thought maybe we would sell.

Q. Did you and Mr. Murphy ever discuss whether you ought to sell them in 1944 and 1945?

A. Well, we talked about it quite a bit. I was always against selling them. I told Mr. Murphy, I says, "You don't want ever to come down Lakewood Boulevard and say, 'I used to own that property.'" And that is just exactly what happened. I was against selling the property from the start.

Q. What finally convinced you, or why did you finally consent, at least, to sell them?

A. We got so much advice from Mr. Boland, Mr. Boland was so persistent on what they could do, the prices he could get, and naturally there was quite a profit on them, and they just finally overrode me, that's all.

Q. Did you discuss the tax consequences of selling these with anybody? [474] A. No, sir.

Q. You say no? A. No, sir.

Q. With respect to the 100 duplexes, when those were built, did you have any then intention concerning those different than the 70? A. No, sir.

Q. Or the 22? A. No, sir.

Q. What was your intention toward those?

A. The same thing, a permanent investment.

(Testimony of Edward Pool.)

Q. Which were sold first, if you know?

A. I think the 70 was sold.

Q. Who was authorized to sell them for you?

A. Mr. Boland.

Q. At the time you gave permission to sell the 70, did you also give permission to sell the 100?

A. No, sir.

Q. Were you asked to give permission?

A. Yes, sir.

Q. What was your answer?

A. I just didn't want to sell them.

Q. What happened? What finally convinced you to sell the 100?

A. Well, it was just, as I say, the pressure was put on [475] me about the high prices and how quick they could sell them, how quickly they could be financed, and how quickly you could get rid of them and put the money in something that would pay a better return, because we wasn't getting the income we should have got on that much of an investment. [476]

Q. Do you mean on that much of an investment or on that price, the market price?

A. That is what I mean, the market value of the buildings.

Q. What did you do with the money that you got out of the 70 and the 100?

A. Put it in the stock market.

Q. All of it? A. I think I did, yes.

Q. How long were you actively working for

(Testimony of Edward Pool.)

Aircraft Builders in the sense that you came to the office regularly? Do you go down there now?

A. Oh, no.

Q. When did you cease going to the office regularly?

A. I ceased going to the office regularly a good while ago.

Q. Can you identify it any closer than that?

A. We practically quit building I think it was in 1945, along there some time, and didn't—I used to go down occasionally, you know, maybe once or twice a week. I was out of town a great deal. I was out of town I think all the time while they were selling that 70. I just went back East.

Q. Do you remember signing deeds to any of these properties?

A. Oh, yes, we would sign the deeds for them. When I [477] would come in, they had certain deeds for me to sign. Whatever they wanted me to sign, she had those laid out for me.

Q. Were the deeds filled out when they were signed, do you know? A. I think they were.

Q. Were they always filled out?

A. I think there was some I signed that wasn't filled out and that Mr. Murph, wasn't going to sign. She used to keep them where they would need one signature or the other.

Q. Did you ever raise any question about that procedure?

A. No. Mr. Swaffield said that was perfectly

(Testimony of Edward Pool.)

all right as long as everybody signed in the presence of Mrs. Woodruff.

Q. Who was Mr. Swaffield?

A. He was our attorney.

Q. Do you recall when the plans and specifications for the 22 apartments and the 70 were being prepared? A. Yes.

Q. Did they differ in any respect from the type of thing you had been building before?

A. I don't know whether the specs actually differed or not.

The Court: What differed?

The Witness: The specifications, the FHA, you know. You have what they call M.C.R. and you can make them [478] as much better as you care to.

Q. (By Mr. Axelrad): What is M.C.R.?

A. Minimum construction requirements demanded by FHA. You can go as much better as you care to.

Q. Did you go any better?

A. Yes, quite a bit.

Q. In what specific ways?

A. I insisted on a different caliber of work with the thought of holding them.

Q. What kind of work had to be better?

A. For instance, one of the things that is very important for it is a good plaster job, a good base, a good full three-quarters job, instead of seven and five-eighths that they use. I insisted on a good darby and rodded job. That is, I insisted on all the rooms being taken care of that way, instead of the

(Testimony of Edward Pool.)

usual way of slapping it on and smoothing it off and letting it go.

Q. And would the kind of thing you would insist on make it an easier kind of building to sell, in your opinion?

A. No, because the public don't see any different in that. It is just a better constructed, sounder building. My idea was renting and taking care of it, because a rental apartment, you know, takes a pretty good beating. We had to rent to children, too, you know. [479]

Q. Are there any other specific ways in which these buildings were different from the kind of thing you had been doing before?

A. For instance, all party walls, I insisted those be in a different manner than what I did in the other ones. There were quite a lot of differences all the way around, interior finish, painting, and enameling work.

Q. What kind of floors did you have in these houses? A. Oak, hardwood floors.

Q. What kind of roofs?

A. A composition roof.

Q. How long would a composition roof be good for?

A. The average composition roof is supposed to be a 20-year roof. It has to be guaranteed roof or FHA won't approve it.

Q. At the time you disposed of the 100 or agreed to dispose of them, was any request made to have you sell the 22 apartment buildings?

(Testimony of Edward Pool.)

A. They were always trying to get permission to sell them. They seemed to be working on me, because I was the one that was against it all the time.

Q. Was Mr. Murphy anxious to sell them?

A. He got rather enthusiastic as the price went up, you know, but I still didn't want to sell them. I didn't want to sell the buildings because I knew what could happen. [480]

Q. What could happen?

A. Just as I say, you get a good piece of income in a good location, and you sell them and you just can't make as good a buy again, for instance, with the same rent that you can get out of the rental income.

Q. Was the rental income that you were getting enough income for you?

A. It was for me, for what we had put in the buildings, yes.

Q. To give you enough to live on, do what you want to do? A. It was a lovely setup.

Q. What happened with the money you got as a result of selling these?

A. I put it in the stock market.

Q. And then what happened?

A. I think I lost some money in the stock market.

Q. Do you still have stock holdings?

A. No, not now. Well, I have in other Artcraft companies.

Q. What happened to them?

A. Well, they——

(Testimony of Edward Pool.)

Q. Did they make money or lose money?

A. I don't know how it will ultimately wind up.

Q. How are they now? [481]

A. They are not so hot, as you say.

Q. Was this one of the fears you had in disposing of these properties?

A. That's right. Just like I didn't want to go out of town, and I went out of town.

Q. What do you mean?

A. I didn't want to go out of town on these jobs. I thought we ought to stay where we belong, where we knew the building business, and that is here. We should have stayed here, not go out of town, just because we know how to build. That is the reason I was against going out of town, which is a matter of record, as far as that goes. I didn't want to go at all, just like I didn't want to sell the income property.

Q. When were the 22 apartments finally sold, if you know?

A. I think that was the last ones that were sold.

Q. Do you know what year or years?

A. Well, that was quite a while after we quit, I think. I think that was around 1948 or 1949, something like that.

Q. Do you know why you sold those?

A. Well, then the rental had slackened off, I was discouraged and I did not care, because I had been overridden on the others. All we had to do on those was drop the rent just a trifle and we could have filled them right [482] up. It was a good in-

(Testimony of Edward Pool.)

vestment. There is no question about that. The location will always be a good one.

Q. Do you still own the market building?

A. Yes, sir.

Q. Was there any effort made to sell that?

A. No, sir.

Q. Any effort made by anybody to buy it?

A. Oh, yes, several times. It is a good location.

Q. Why have you refused to sell that?

A. I simply declared myself, that's all.

Q. You were firmer about it than you were about the others?

A. Yes, or it would have been gone, too.

Q. When Mr. Boland was selling the 70 duplexes and the 100 duplexes, were you down at the office on any occasion? A. Occasionally.

Q. Did you ever assist him? A. No, sir.

Q. Do you know whether Mr. Murphy was assisting him?

A. I don't know. I wasn't there all the time.

Q. I hand you Respondent's Exhibit YY, which is a photostatic copy of a real estate page in the Los Angeles Times for Sunday, August 7th, and I point to this advertisement in the lower left-hand side, which says, "For sale, 50 [483] duplexes, $13,000," and at the bottom appears, "Artcraft Builders, Inc., Good Homes."

Do you know anything about that advertisement?

A. No, sir.

Q. Did you ever see that or similar kinds?

(Testimony of Edward Pool.)

A. No, I never seen it. I was in the East mostly when those ads were running.

Q. Did you authorize the use of the name "Artcraft?" A. No, sir.

Q. If it had been pointed out to you, would you have thought anything of it, one way or the other?

Mr. Chehock: I object to that as hypothetical. That isn't the question here.

Mr. Axelrad: It is hypothetical, your Honor, but I think that——

The Court: I don't think it will amount to anything, because he very obviously didn't give any thought to it, and now he would be just giving his opinion as to what he might have done back in those days.

Mr. Axelrad: Withdraw the question, your Honor.

Q. (By Mr. Axelrad): We have here other advertisements of a similar nature. Here is one, for instance, that goes a little further. It says it is the builder that is selling them, and then it says, "Artcraft Builders, Inc." Is that the fact? [484]

A. No.

Q. Was Artcraft selling them?

A. No. Artcraft had nothing to do with them.

Q. Did Artcraft own them?

A. No. Artcraft didn't own them.

Q. What was Artcraft's relationship to these duplexes that were being sold at that time?

A. None whatsoever that I know of, other than that they were the original builders of them.

Q. Did you and Mr. Murphy and your wives

(Testimony of Edward Pool.)

pay Artcraft any money during this period for anything?

A. No. Oh, I think for renting them and taking care of them and servicing them, yes, acting as the agent for them.

Q. The rental agent? A. Yes.

Q. Do you know whether that included the market building as well?

A. That included all our holdings.

Q. Was there anything different in the way you got your money from the market building than from the duplexes?

A. I remember at the time the leases were made out, and the original leases were made out to the market building in the four names, and the market insisted on making the checks to the Associates and not to Artcraft.

The Court: Did you have one tenant in the market [485] building?

The Witness: No, sir.

The Court: How many were there?

The Witness: There were three. But the Alpha Beta Market is the dominating tenant, the big tenant.

Q. (By Mr. Axelrad): What kind of a lease do you have with Alpha Beta Market?

A. A percentage lease.

Q. What do you mean by that?

A. You get a percentage of the amount that they take in on the various departments, like meats and groceries.

(Testimony of Edward Pool.)

Q. During the period from 1943 or 1944 through 1950, when you held part or all of these departments, did you hold them for sale to the public prior to putting them on the market for liquidation?

A. They were never built for that idea at all.

Q. Did you ever consider yourself as having built those for sale? A. No, sir.

Mr. Axelrad: That's all.

Cross Examination

Q. (By Mr. Chehock): Mr. Pool, I think you testified on direct examination you have been a builder all your life. [486] A. Yes, sir.

Q. Were you a builder of houses for sale on your own account? I mean, did you build the houses and then have them sold?

A. It was contracted, mostly, and then they would, as you say, you go out and spec on a half-dozen good lots.

The Court: What do you mean, "spec?"

The Witness: When you build them and they are not contracted for previously, you know, until you finish them, and then you sell them on the market to people who come along and buy them.

Q. (*By Mr. Axelrad*): In other words, you build them yourself and sell them, and you made the profit on them yourself? A. Yes, sir.

Q. How much of that did you do?

A. Not so much. In other words, when we moved to Long Beach, we built quite a few homes, you know what I mean, in tracts and built them

(Testimony of Edward Pool.)

and sold them as we built them. They really were speculative. They were not contracted for prior to starting.

Q. You are talking about Arteraft now, are you?

A. Yes, sir.

Q. I am talking about your own private enterprises prior to Arteraft. You said you were a builder all your life. [487] A. That's right.

Q. What do you mean by that?

A. I built residential properties all my life, individual homes and rental units.

Q. Did you sell them and make a profit on what you sold? A. Yes.

Q. Or did you build them on contracts for others?

A. Both. The only time I would build for the market, as we say, speculatively, is when you would happen to hit a half-dozen or a dozen real good lots, good locations.

Q. How many houses would you estimate, prior to Arteraft, you had built and sold on your own account and made the profit yourself, or the difference between the cost and the selling price?

A. I couldn't tell you.

Q. Just approximately.

A. You mean over the years?

Q. Yes, up to the time Arteraft was formed in 1941.

A. I haven't the least idea. I built hundreds of homes in Cincinnati.

Q. I am not talking about the homes you built on

(Testimony of Edward Pool.)

contract, but I am talking about the homes you built on your own account and sold them and made the profit on the difference between the cost of building to you and the selling price. [488]

A. Well, I wouldn't be able to tell you back over the years, because the majority of the work naturally is sold prior to starting unless, as I say, you hit a good spot, some good lots you buy, and then you build them and sell them to the market, individual homes.

Then I can say this, I never in all those years ever built any income for specs, if that is what you mean.

Q. You built them for sale?

A. The only income I would build would be for an individual who wanted me to build an income building for him as an investment. In other words, I did not build income for speculation, because it is too hard to finance, and the building associations think they are going in business with whoever owns them. What you are saying is that in building enterprises the profit you made was either by building on contract for someone else, or it was building them on your own account.

A. That is correct.

Q. Selling them and making a profit, is that right? A. That is correct.

Q. Would you say you had built on your own account, sold them and made a profit on them, several hundred houses prior to 1941?

A. Over the years, I would say yes.

(Testimony of Edward Pool.)

Q. Artcraft Builders, Inc. never was liquidated, was it? [489] A. No, sir.

Q. It is still in existence, isn't it?

A. Yes, sir.

Q. In regard to these 70 duplexes and 100 duplexes here in controversy on Tracts 11451 and 13163, the FHA loans there exceeded the cost of building, including land and everything else, subdivision, isn't that true? A. I think so.

Q. So actually when you testify about all these extras that were put in the 70 duplexes and the 100, that was not really money that you or Mr. Murphy had to pay, was it?

A. I don't know that——

Q. You had no money of your own actually invested in the 70 and 100, did you?

A. I think we bought the ground first for Artcraft. I am not sure of that. But you understand your differential, the reason you beat the loan, and you got that portion—in those days they were Title 6, and they were loaning 110 per cent, and then it was up to the builder to see if he couldn't beat it. The more he could beat it, the better they liked it, and the better the financial institutions would finance you, because they knew it was a safe deal if you could beat a loan. [490]

Q. Whatever money was used in building the houses was money that you borrowed from FHA?

A. That's right.

Q. Rather than your own funds.

A. That is correct.

(Testimony of Edward Pool.)

Mr. Chehock: I think that's all.

Mr. Axelrad: Just one or two questions.

The Court: I don't understand. You borrowed the money from FHA, you say?

The Witness: No, sir.

The Court: You borrowed it under the FHA plan you mean.

The Witness: They insured the loan.

The Court: All right.

Mr. Axelrad: I have just one or two questions.

Redirect Examination

Q. (By Mr. Axelrad): These houses you are telling about having built on spec, as you call it, prior to coming to Los Angeles and Southern California, was that all in Cincinnati?

A. Yes, sir.

Q. How did you sell them? Did you sell them personally?

A. No, sir. I never sold any houses personally. I sold them through brokers.

Q. In every case? [491]

A. All the time, because you don't want to get the brokers against you. They won't show your house or let anyone look at it for you to sell it otherwise.

Q. It wasn't good business?

A. It is very bad business to sell your own house.

Q. Is that why you used a broker to sell the 22 apartments?

A. That was standard procedure with me.

(Testimony of Edward Pool.)

Q. Did you consider a broker added anything? You paid them a lot of money.

A. I know that. There is a lot of work to it, too. I don't want to be bothered with it.

Q. Did you know anything about it?

A. Not selling, no. I know how to build them, but then I turn them over to somebody else to get rid of them.

Q. There is a sort of saying in Southern California that anybody can be a builder. Do you think that is true? A. No, I don't.

The Court: You are asking the wrong person that question.

Mr. Axelrad: That is the answer I wanted, your Honor.

The Court: You wouldn't very likely get a different answer.

Mr. Axelrad: It is a true answer, too. [492]

Q. (By Mr. Axelrad): When the 100 duplexes were placed on the market, did you have any discussions with anybody about whether it was time to sell them from a tax point of view?

A. No, sir.

Q. Did you ever give instructions to hold a sale date up for a given time?

A. No, sir. I knew nothing about the office work. I had nothing to do with that.

Q. Were you ever consulted about such a question? A. No.

Mr. Axelrad: That's all, I think.

(Testimony of Edward Pool.)

The Court: Any other questions?

Mr. Chehock: Let me ask one more question.

Recross Examination

Q. (By Mr. Chehock): You say you were against the selling of these 70 and 100 duplexes.

A. Yes.

Q. Since that time there have been a couple other Artcraft corporations formed, haven't there, one in New Mexico and one in Colorado?

A. Yes, sir.

Q. Those corporations have built homes?

A. Yes, sir. [493]

Q. For sale? A. Yes, sir.

Q. They are not being retained?

A. No, sir.

Q. Is it your feeling that those should have been retained for income purposes?

A. They are individual houses. That is very poor income, very poor investment.

Mr. Chehock: That's all.

The Court: Anything else?

Mr. Axelrad: That's all.

The Court: You are excused.

(Witness excused.)

Mr. Axelrad: Your Honor, I would like permission at this time to remove certain exhibits for the purpose of having photostats made and substituting the photostats for the originals, and also so that we will have copies for counsel.

The Court: That may be done.

Mr. Chehock: Your Honor, just to be sure, I think they are all in evidence, but I would like to offer in evidence Exhibits A through III, inclusive, in the event through some slip-up they haven't been put in evidence.

The Court: What do you mean? Are they attached to the Stipulation? [494]

Mr. Chehock: No. These are exhibits in the case that were identified, but if for some reason they weren't put in, I would like, in the event there has been a slip-up, to ask that they be received in evidence.

The Court: All the exhibits that were offered here in the course of this trial as exhibits, I mean aside from the stipulation, have been admitted.

Mr. Chehock: That's all I wanted to be sure of.

The Court: You read off a series of returns and so forth, and although it is a bit monotonous, I took the pains to say after each one that it would be admitted. I remember that.

Mr. Chehock: We have been through the alphabet twice and are into the third one, and I thought there might be a slip-up, but if there hasn't been, that is all right. I wanted to be sure they are in.

The Court: All right. I can assure you all of those offered here are in, and those attached to the Stipulation, the Stipulation is received and made part of the record.

Mr. Chehock: All right.

The Court: Anything else?

Mr. Chehock: I would like to move to withdraw the exhibits, Respondent's Exhibits C, D, E, F, I,

J, K, L, and all exhibits from S through III, inclusive, for [495] photostating, so that they can be substituted.

The Court: That may be done.

Mr. Chehock: Are the Petitioners resting?

Mr. Axelrad: The Petitioners rest, your Honor.

The Court: And the Respondent?

Mr. Chehock: The Respondent rests.

The Court: How much time you want for briefs and how do you want it? Is there any preference?

Mr. Axelrad: I assume the Petitioners will either file the first brief or there will be simultaneous briefs. I always like to write the second brief.

The Court: You are on the wrong side of the fence for that.

Mr. Axelrad: I guess that is so.

Mr. Chehock: I wouldn't mind simultaneous briefs, but I would like quite a bit of time.

The Court: I think in this case I would like simultaneous briefs and then I will have a reply from each of you, of course. That is the only objection where the Petitioner has the burden of filing the first brief and then the last one. So we will have simultaneous briefs and then a reply from each.

How much time to you want? I can give you as much as you want. I would rather give it now than to have a lot of motions coming in for extension of time, except for the [496] fact that sometimes I am going to get motions for extensions, anyhow.

How about 60 or 90 days?

Mr. Chehock: I would like 90 days.

Mr. Axelrad: That will be all right.

The Court: 90 days, and 45 days for reply.

Mr. Chehock: Thank you.

Mr. Axelrad: Thank you.

The Court: The case will stand submitted on filing of briefs.

Now the court will recess and we will come back at 2:15, those who have further matters here.

The Clerk: That will be June 4th for the first brief, and September 17th for the reply briefs.

(Whereupon, at 1:00 o'clock p.m., Wednesday, March 5, 1953, the hearing in the above-entitled matter was closed.)

[Endorsed]: T.C.U.S. Filed March 24, 1953.

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[Endorsed]: No. 15399. United States Court of Appeals for the Ninth Circuit. Edward Pool and Lottie Pool, Edward Pool, Lottie Pool, William K. Murphy, Edna Murphy, William K. Murphy and Edna Murphy, Petitioners, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petitions to Review Decisions of the Tax Court of the United States.

Filed: December 20, 1956.

Docketed: December 27, 1956.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

Docket No. 15399

EDWARD POOL et al., Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

## STATEMENT OF POINTS

Now come the petitioners on review in the above-entitled cause, by their attorney, Irving I. Axelrad, and state that they intend to rely on the following points:

1. That the Tax Court erred in holding and deciding that certain apartment buildings and duplexes admittedly used in petitioners' trade or business had also been held primarily for sale to customers in the ordinary course of petitioners' trade or business, and, therefore, the proceeds of the sale were not entitled to the capital gain treatment authorized by Sec. 117(j) of the Internal Revenue Cole of 1939.

2. That the Tax Court erred in entering final orders and decisions that there were deficiencies in petitioners' income taxes in the amounts and for the years, as follows:

| | | |
|---|---|---|
| Edward Pool and Lottie Pool | 1948 | $18,651.22 |
| William K. Murphy | 1946 | 3,410.79 |
| William K. Murphy | 1947 | 98,401.48 |

| | | |
|---|---|---|
| Edna Murphy | 1946 | $ 3,410.79 |
| " " | 1947 | 98,401.49 |
| Edward Pool | 1946 | 5,697.02 |
| " " | 1947 | 86,828.50 |
| Lottie Pool | 1946 | 5,697.02 |
| " " | 1947 | 86,828.50 |
| William K. Murphy and Edna Murphy | 1948 | 17,349.60 |

3. That the Tax Court erred in that its decisions are not supported by the evidence.

4. That the Tax Court erred in that its decisions are contrary to the law.

/s/ IRVING I. AXELRAD,
Attorney for Petitioners

[Endorsed]: Filed January 2, 1957. Paul P. O'Brien, Clerk.

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[Title of Court of Appeals and Cause.]

## DESIGNATION OF RECORD

Come now the petitioners in the above-entitled cause, by their attorney, Irving I. Axelrad, and designate, for printing of the record, as follows:

The petitioners have prepared and submitted to the Respondent a Joint Motion for Consolidation and for Dispensing With Printing of Exhibits and Records, a copy of which is attached hereto. It is anticipated that said Joint Motion will shortly be submitted to the Court and, in the event the orders

therein requested are granted, the Petitioners designate the following:

1. Docket entries, Tax Court Docket Number 36108.

2. Petition, Tax Court Docket Number 36108.

3. Respondent's Answer, Tax Court Docket Number 36108.

4. Minutes of hearing of December 3, 1952.

5. Minutes of Trial of February 27, 1953, and March 2, 3 and 4, 1953.

6. Stipulation of Facts.

7. Transcript of Trial of February 27, 1953.

8. Transcript of Trial of March 2, 1953.

9. Transcript of Trial of March 3, 1953.

10. Transcript of Trial of March 4, 1953.

11. Memorandum of Findings of Fact and Opinion.

12. Decisions, Tax Court Dock Numbers 36108, 36109, 36110, 36111, 36112 and 36113.

13. Petition for Review, Tax Court Docket Number 36108.

14. Proof of Service, Tax Court Docket Number 36108.

15. Designation of Contents of Record on Review, Tax Court Docket Number 36108.

16. Order enlarging time for filing transcript of record.

17. Joint motion for consolidation and for dispensing with printing of exhibits and records.

18. Petitioners' Statement of Points.

19. This Designation of Record.

In the event the said Joint Motion is not granted, it will be necessary for Petitioners to file another designation.

/s/ IRVING I. AXELRAD,
Attorney for Petitioners

[Endorsed]: Filed January 2, 1957. Paul P. O'Brien, Clerk.

In the United States Court of Appeals
for the Ninth Circuit

No. 15399

Tax Court Docket No. 36108

Edward Pool and Lottie Pool, Petitioners on Review, vs. Commissioner of Internal Revenue, Respondent on Review.

Tax Court Docket No. 36109

Edward Pool, Petitioner on Review, vs. Commissioner of Internal Revenue, Respondent on Review.

Tax Court Docket No. 36110

Lottie Pool, Petitioner on Review, vs. Commissioner of Internal Revenue, Respondent on Review.

Tax Court Docket No. 36111

William K. Murphy, Petitioner on Review, vs. Commissioner of Internal Revenue, Respondent on Review.

Tax Court Docket No. 36112

Edna Murphy, Petitioner on Review, vs. Commissioner of Internal Revenue, Respondent on Review.

Tax Court Docket No. 36113

William K. Murphy and Edna Murphy, Petitioners on Review, vs. Commissioner of Internal Revenue, Respondent on Review.

## JOINT MOTION FOR CONSOLIDATION AND FOR DISPENSING WITH PRINTING OF EXHIBITS AND RECORDS

Come now the parties in each of the above entitled causes, by their respective attorneys, and re-

quest the Court to issue the following orders for purposes of facilitating the hearing and decision of the above entitled causes:

1. That the above entitled causes be consolidated for purposes of briefing, hearing and decision under the title of Edward Pool and Lottie Pool, et al. vs. Commissioner of Internal Revenue.

2. That the documents designated and included in the transcripts of record on review in the five causes bearing Tax Court Docket Numbers 36109, 36110, 36111, 36112, and 36113 not be printed, but that only the full and complete transcript of record in the case of Edward Pool and Lottie Pool vs. Commissioner of Internal Revenue, Tax Court Docket No. 36108, including, inter alia, the documents which relate to all of the cases, shall be printed, omitting, however, the printing of Joint Exhibits 1-A through 18-R, Petitioners' Exhibits 19 through 30, and Respondent's Exhibits AA through III; and that all such transcripts of record on review and Exhibits not printed shall be considered for all purposes as a part of the printed record herein and may be referred to by counsel in their respective briefs and on oral argument, or reproduced in whole or in part in an Appendix to their respective briefs, and considered by the Court with the same force and effect as if actually included in the printed record on review filed herein.

3. That the decision of this Court in the case of Edward Pool and Lottie Pool, Tax Court Docket

Number 36108, shall be the decision of this Court in the other five related cases bearing Tax Court Docket Numbers 36109, 36110, 36111, 36112 and 36113; but that a separate judgment be entered in each of the six cases.

/s/ IRVING I. AXELRAD,
Attorney for Petitioners

/s/ CHARLES K. RICE,
Assistant Attorney General,
Tax Division, United States,
Attorney for Respondents

So ordered:

/s/ WM. HEALY,
Chief Judge

/s/ WALTER L. POPE,

/s/ FREDERICK G. HAMBLY,
United States Circuit Judges

[Endorsed]: Filed January 10, 1957. Paul P. O'Brien, Clerk.

LIBRARY
SUPREME COURT, U. S.

IN THE

# Supreme Court of the United States

October Term, 1957
No. 856

EDWARD POOL and LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY and EDNA MURPHY,

*Petitioners,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

**Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.**

IRVING I. AXELRAD,
6399 Wilshire Boulevard,
Los Angeles 48, California,
*Attorney for Petitioners.*

*Of Counsel:*
MITCHELL, SILBERBERG & KNUPP,
6399 Wilshire Boulevard,
Los Angeles 48, California.

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IN THE

# Supreme Court of the United States

October Term, 1957

No. .....

EDWARD POOL and LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY and EDNA MURPHY,

*Petitioners,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE.

## Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

Edward Pool, Lottie Pool, William K. Murphy, and Edna Murphy, petitioners, pray that a writ of certiorari issue to review the judgment of the Court of Appeals for the Ninth Circuit entered in this case.

### Opinions Below.

The memorandum findings of fact [R. 29-70] and opinion [R. 70-88] of the Tax Court are not officially reported. The opinion of the Court of Appeals (Appendix, *infra*, pp. 1 to 34) has not yet been reported.

## Jurisdiction.

The judgment of the Court of Appeals was entered on December 18, 1957. The jurisdiction of the Court of Appeals rested on Sections 7482 and 7483 of the Internal Revenue Code of 1954. The jurisdiction of this Court is invoked under 28 U. S. C. 1254.

## Question Presented.

The taxpayers were the owners of approximately 200 duplex apartment buildings which were originally acquired and held for rental to tenants. Later, the taxpayers having decided that it would be better to liquidate this investment because of changed circumstances, the properties were sold on an individual basis. In connection with the sales, the taxpayers engaged in no activities except those consistent with an attempt to sell the properties, in their existing condition, as expeditiously as possible and at the best possible prices.

The question presented is whether such liquidation constituted the conduct of a business so that the property, formerly held as a capital investment, became property held primarily for sale to customers *in the ordinary course of a trade or business,* as that term is used in Section 117(j)(1)(B) of the Internal Revenue Code of 1939, and so that property was no longer eligible for capital gains taxation.

## Statute and Regulations Involved.

Internal Revenue Code of 1939:

"Section 117(j) [as added by Section 151(b) of the Revenue Act of 1942, c. 619, 56 Stat. 798, and amended by Section 127(b) of the Revenue Act of 1943, c. 63, 58 Stat. 21] *Gains and Losses from Involuntary Conversion and from the Sale or Exchange of Certain Property Used in the Trade or Business.*

"(1) *Definition of property used in the trade or business.* For the purposes of this subsection, the term 'property used in the trade or business' means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(1), held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not (A) property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year, or (B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business. . . .

"(2) *General Rule.* If, during the taxable year, the recognized gains upon sales or exchanges of property used in the trade or business, plus the recognized gains from the compulsory or involuntary conversion (as a result of destruction in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation or the threat or imminence thereof) of property used in the trade or business and capital assets held for more than 6 months into other property or money, exceed the recognized losses from such sales, exchanges, and conversions, such gains and losses shall be considered as gains and losses from sales or exchanges of capital assets held for more than 6 months. . . ." (26 U. S. C. (1946 Ed.), Sec. 117.)

Treasury Regulations 111, promulgated under the Internal Revenue Code:

> "Section 117(j) provides that the recognized gains and losses
>
> "(a) from the sale, exchange, or involuntary conversion of property used in the trade or business of the taxpayer at the time of the sale, exchange, or involuntary conversion, held for more than six months, which is
>
> "(1) of a character subject to the allowance for depreciation provided in section 23(1), or
>
> "(2) real property,
>
> provided that such property is not of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year, or is not held by the taxpayer primarily for sale to customers in the ordinary course of trade or business, . . . shall be treated as gains and losses from the sale or exchange of capital assets held for more than six months if the aggregate of such gains exceeds the aggregate of such losses. . . ."

## Statement.

The Tax Court [R. 33-70] made detailed findings of fact, both with respect to the issue here presented and another issue which is no longer in controversy.

Some of the facts were subject to a stipulation. [R. 17-29.] The remaining facts were established by testimony and exhibits. For purposes of this petition for writ of certiorari, the material and undisputed facts may be summarized as follows:

The taxpayers, Edward Pool and his wife, Lottie Pool, William K. Murphy and his wife, Edna Murphy, early in 1944 formed a joint venture known as "Edward Pool

and Associates" (sometimes referred to as "Associates"). [R. 46-47.]

On March 31, 1944, Associates acquired 70 duplexes and 22 new apartments which had been constructed for the taxpayers by Artcraft Builders, Inc., a corporation, in which the individual taxpayers were then the sole stockholders. [R. 44-46.] In March, 1946, the taxpayers also acquired an additional 100 duplexes which had similarly been constructed for them by Artcraft. [R. 52.] The 22 apartments, the 70 duplexes, and the 100 duplexes, respectively, were leased to tenants as they were completed. The initial leases were all written and were for a period of one year, at a minimum. The taxpayers utilized Artcraft as its rental agent; Artcraft entered into leases, collected the rent, kept books, paid bills and generally managed the property and was compensated for the services which it rendered. [R. 21-22, 55-56.]

The individual taxpayers acquired these properties as an investment, *i.e.*, to hold them for the production of rental income.[1]

Although the taxpayers had rejected previous offers and had refused to sell some of the properties, by the beginning of 1946, economic conditions had substantially changed; with the return of servicemen, the market price of houses in southern California had begun to rise, while, at the same time, the rentals which the taxpayers could obtain were frozen under rent control. [R. 54-57.] From the beginning of 1946, one Boland, a real estate broker, had attempted to influence the taxpayers to permit him to sell the 22 apartments and the 170 duplexes. Although the taxpayers, at first, decided against selling any of the

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[1]See footnote 4, *infra*, page 11.

properties, they were later persuaded to permit Boland to sell the 70 duplexes, but they still refused to sell the 22 apartments and the remaining 100 duplexes. He was given permission to sell the 70 duplexes sometime in May of 1946. [R. 57-58.]

Boland agreed to accept a commission of $500.00 a duplex, out of which he agreed to pay all of the expenses of sale, such as advertising, other salesmen and clerical help. He was given the right, however, to use Artcraft's office, telephone and had part-time use of Artcraft's secretary. He advertised the property (sometimes using Artcraft's name although he knew Artcraft was not selling the houses); employed several salesmen of his own, wrote the contracts, initiated the escrows, checked credit and did everything necessary to sell the properties. Boland succeeded in taking deposits or closing the transactions on the sale of all 70 of the duplexes within a ten week period of time. [R. 58-60.]

Sometime after completing these transactions, Boland succeeded in inducing the taxpayers to consent to the sale of the remaining 100 duplexes, although they still refused to sell the 22 apartments and a market building which they had acquired. Boland sold the 100 duplexes in much the same manner as he had previously sold the 70 duplexes. All but 20 of them were sold by the end of 1946, and the remaining duplexes were sold early in 1947. [R. 60-63.]

In connection with all the sales, the activities of taxpayers, individually, were minimal. [R. 59-60.] They were confined for the most part to the signing of the necessary papers and, in connection with financing the sale of some of the duplexes, Murphy spent some time in arranging for alternate financing when difficulties were encountered. [R. 61.]

The proceeds of the sales were invested by the parties, principally in securities, although some of the money was used for an investment in a building which contained a bank and six retail stores. This building was built in 1948 and was held for rental purposes until 1952 when it was disposed of in a forced sale under threat of foreclosure. [R. 210-213, 514.]

The Tax Court made the following, ultimate conclusions [R. 70]:

> "Beginning with the employment of Boland, the four individual petitioners herein began a business of selling real estate, and from April 1946 the 70 duplexes on Tract 11451, and from July 1946 the 100 duplexes on Tract 13163 were held by them primarily for sale to customers in the ordinary course of that business."

The Court of Appeals, affirming the Tax Court, ruled that the taxpayers, in making the sales, did so [R. 565] "as a part of the taxpayers' business," and decided that the Tax Court was correct in holding that Section 117(j)(1)(B) of the Internal Revenue Code of 1939 was applicable, that the taxpayers were not entitled to the benefits of capital gain taxation and, instead, that the profits were taxable as ordinary income.

## Reasons for Granting the Writ.

The Court of Appeals for the Ninth Circuit has erroneously decided an important and recurring question arising under the Internal Revenue laws in such a manner as to be in direct conflict with decisions of the Courts of Appeals for the Third, Seventh, and Eighth Circuits.

The issue, on which the Courts have divided, concerns the proper interpretation of Section 117(j)(1)(B) of the

Internal Revenue Code of 1939 (identical, in pertinent part, with Section 1231(b)(1)(B) of the Internal Revenue Code of 1954), which denies capital gain taxation with respect to depreciable property and real property used in a trade or business if it is "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."[2]

The Court below has decided that, even though property is originally acquired and held by a taxpayer for a purpose other than sale to customers in the ordinary course of a trade or business—here as an investment in rental properties—a subsequent decision to liquidate the investment[3] and a course of conduct to effectuate that decision, permits the factfinder to conclude that, regardless of the purpose for which the property was previously being held, at the time of sale the property is being held by the taxpayer for sale to customers in the ordinary course of his trade or business *even though the taxpayer engages in no conduct except that consistent with an attempt to sell the property, in its existing condition, as expeditiously as possible and at the best possible prices.*

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[2]The identical language also appears in Section 117(a)(1)(A) of the 1939 Code and in Section 1221(1) of the 1954 Code so as to exclude from the definition of a capital asset "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."

[3]To avoid repetition of the full statutory language we will sometimes use the term "investment" or "investment property" to connote the antithesis of the phrase "property held primarily for sale to customers in the ordinary course of his trade or business." The term "investment property" is, itself, capable of conveying different meanings. However, notwithstanding this and even though the term has not appeared in the statute after its use in Section 206 of the Revenue Act of 1921, the courts continue to use the phrase in somewhat the same manner as we employ it here. See Miller, The "Capital Asset" Concept: A Critique of Capital Gain Taxation, 59 Yale L. J. 837, 838 (fn. 9).

## I.

## The Decision of the Ninth Circuit Is in Conflict With Decisions of the Courts of Appeals for the Third, Seventh, and Eighth Circuits.

In *Curtis Company v. Commissioner*, 232 F. 2d 157, reversing the Tax Court (23 T. C. 740) the Court of Appeals for the Third Circuit (Judge McLaughlin dissenting) interpreted and applied Section 117(j)(1)(B) precisely opposite to the manner in which the Court below has construed that section. The taxpayer there was in the business of building new homes for sale (it was the largest builder of homes in the Philidelphia area) and was also in the business of building and renting homes and apartments. During the years 1942 through 1944, the taxpayer had constructed a large number of single family homes and duplex apartments for rental purposes. In 1946, after government restrictions were removed on the resale of housing built with priority assistance, but when restrictions were still in existence regarding rents which could be charged, the taxpayer decided to sell the houses and duplexes because it was convinced that they had appreciated as much as they would and because this was an opportune time to sell.

The taxpayer, in *Curtis*, made the sales of the properties by using its own staff of salesmen, who were paid on a commission basis. Newspaper advertisements were utilized to attract potential buyers. The sales were made during a four year period (1947-1950). Simultaneously, during those years, the taxpayer was also engaged in selling houses which it had constructed for resale and it reported the profits on such sales as ordinary income. However, it reported capital gain on the sale of the units originally constructed for rental purposes.

The Tax Court (23 T. C. 740), finding that the taxpayer was simultaneously engaged in the business of building houses for sale and of building and holding houses for rent, and finding that the particular units sold during the tax years had been held for rental purposes up until the time that it was decided to sell them, concluded that the manner in which the rental properties were sold (pp. 752-753) "put it into the business of holding them for sale to customers in the ordinary course of its business." Pointing to the fact that the taxpayer used its own salesmen and had paid them commissions on the sales, and emphasizing (p. 753), as did the Court below in the present case [R. 539-540, 563-568], the "criteria" of the "frequency and continuity of sales," "the substantiality of sales," the "advertising and sales promotion," the Tax Court concluded that the property had become "property held by the taxpayer primarily for sale to customers in the ordinary course of [its] trade or business" and no longer qualified for capital gains taxation.

The Court of Appeals for the Third Circuit disagreed with this interpretation of the quoted statutory language. It held that the activities engaged in by the taxpayer to promote and effectuate the sales did not, within the meaning of the statute, serve to make this a trade or business or to transform the property into that being held primarily for sale to customers in the ordinary course of a trade or business.

Starting with the Commissioner's concession (232 F. 2d 167, 169) that the quoted statutory language would have been inapplicable and that capital gain taxation would have been appropriate if the taxpayer had sold all the properties at one time to one buyer or, indeed, if a firm of brokers had been engaged to sell the properties, the Court of Appeals disagreed with the Commissioner and

the Tax Court in their view that the statute permitted a different result simply because the taxpayer used its own salesmen to effectuate the sales, had conducted an advertising campaign to facilitate the sales, and had a large number of properties to sell (with the consequence that the sales were frequent and extensive), saying (p. 170):

> ". . . We think it a case of one having an investment property on hand which he wants to turn into another form of investment. By the very nature of the case he had to sell the properties a piece at a time. Surely that does not make him a 'dealer' in these parcels of land any more than it would make a man a dealer if he wanted to liquidate his holdings in a corporate stock for which the market was weak so that he had to sell by small parcels instead of by one sale. That is the taxpayer's situation here."

The *Curtis* case is indistinguishable from the present case; indeed, in many respects the facts of the present case present a stronger situation for the inapplicability of Section 117(j)(1)(B).

In essence, both cases present instances where property was originally acquired for *use* and not primarily for sale to customers in the ordinary course of the taxpayer's trade or business.[4] In both cases, the Tax Court concluded

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[4]In the present case the Tax Court concluded [R. 82-83] that Pool's original purpose was to hold the properties for rental purposes; as to Murphy, it was not persuaded that he had any intent other than to rent or sell, depending on what, in the end, should appear to be the most profitable venture. This, quite clearly, is not a finding that Murphy had an original purpose to hold the houses *primarily* for sale to customers in the *ordinary* course of his trade or business. Every investor, we feel safe in saying, has a general purpose to sell his investment at some time if that appears to be most fruitful or profitable.

The Tax Court's decision, as the Court of Appeals noted, was ultimately based on a finding of [R. 563] "an original rental object later changed into sale in the regular course of business."

that, regardless of the original purpose for which the property was acquired, the taxpayers, by attempting to dispose of the property piece-meal, instead of by a single sale, began to hold the property in the conduct of *a trade or business*. The Court of Appeals below, applying the same criteria employed by the Tax Court, concluded that Section 117(j)(1)(B) warranted the Tax Court's determination that these activities constituted the conduct of a trade or business. The Court of Appeals for the Third Circuit, on the contrary, held that the indistinguishable facts in *Curtis* did not constitute a trade or business.

The Court below, it should be noted (p. 541, fn. 6), admitted that *Curtis* embodied a "seemingly contrary conclusion." But, directing attention to some of the earlier decisions of the Ninth Circuit and to Judge McLaughlin's dissent in *Curtis* (232 F. 2d 167, 171-172) where he asserted that the majority's views were in conflict with the decision of other Courts of Appeals, the opinion below refused to accord any "significance" to *Curtis*.[5]

That the *Curtis* case is not a sport within the Third Circuit, but a studied conclusion of that Court regarding the proper meaning of Section 117(j)(1)(B), is emphasized by its subsequent decision in *Philber Equipment Corp. v. Commissioner*, 237 F. 2d 129, which is also in conflict with the decision below. In that case, the Tax Court had determined (25 T. C. 88) that one of the primary purposes for which the property (motor vehicles) was originally acquired was subsequent resale, although the taxpayer also had a purpose of first leasing the vehicles in a rental business. As an alternative ground for its

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[5]In his brief in the Court below, the Commissioner did not attempt to distinguish *Curtis;* indeed, he avoided any mention of it.

decision, it held, as it did in the present case and in *Curtis*, that, regardless of the original purpose of acquisition, the motor vehicles were being held primarily for sale to customers in the ordinary course of the taxpayer's trade or business once their rental use was finished. The Court of Appeals, reversing, not only disagreed with the Tax Court concerning the taxpayer's original purpose, but, what is here important, it rejected the Tax Court's alternative conclusion, saying (pp. 132-133):

> "We cannot subscribe to this 'alternative ground.' To do so would make for judicial nullification of Section 117(j).
>
> "The essence of the Tax Court's alternative ground is that property changes character merely by the fact of its being exposed for sale. We agree with the taxpayer that such a concept is neither logical nor reasonable."

It should also be emphasized that in *Philber* the sales for the corporation were made by a partnership, which was a large scale dealer in motor vehicles and which was composed of the same persons who owned the same proportionate interest in both enterprises. The Court of Appeals, disagreeing with the Tax Court on this score, too, refused to consider that the sales by the partnership justified the conclusion that the corporation was engaged in the business of selling to customers.

We shall not undertake a detailed analysis of the decisions of the Seventh Circuit in *Chandler v. United States*, 226 F. 2d 403, and *Three States Lumber Co. v. Commissioner*, 158 F. 2d 61, or of the Eighth Circuit in *Greenspon v. Commissioner*, 229 F. 2d 947, and *Dillon v. Commissioner*, 213 F. 2d 218, which are also in conflict with the decision below. These decisions make it evident that

both of these Circuits have rejected the principle that activities engaged in by a taxpayer in disposing of investment property can, by themselves, be equated with the conduct of a business so as to make Sections 117(a)(1)(A) or 117(j)(1)(B) applicable. Both of these Circuits have reversed lower courts for having applied the very same standards to which the Court below gave its approval.

There are, to be sure, points of factual difference, as well as factual similarity between the present case and each of the previously cited cases in the Third, Seventh and Eighth Circuits. They do not, however, blur the line of demarcation between the principles being applied by those Courts and the different principles embodied in the decisions below (which accepts the standard fairly consistently applied by the Tax Court). Those Courts do not read Section 117(j)(1)(B) (or its counterpart in Section 117(a)(1)(A)) as embodying a Congressional policy to tax at ordinary income rates the gains realized on the liquidation of investment property, even though the manner of disposition parallels (to a degree) the activities of one who is engaged in a business. The Court below, on the contrary, holds that such activities can constitute a trade or business within the meaning of the above cited statutory provisions.[6]

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[6]The Court below [R. 563], pointing to the fact that one of the four partners (Edward Pool) had, individually, been previously engaged in the business of building and selling houses to customers, and that some or all of the partners had had stock interests in corporations which were engaged in building and selling homes to customers both before and after the tax years here in controversy, held that these circumstances supported the Tax Court's conclusion that the properties, originally acquired as an investment, were held for sale to customers in the ordinary course of a business.

In so holding, the decision below conflicts, in principle, with *United States v. Bondurant*, 245 F. 2d 265 (C. A. 6th), where it was held that, although an individual was in the business of

## II.

## The Question Presented Is an Important, Recurring Issue Warranting Review by This Court.

The question raised by the decision of the Court below is an important, recurring one under the Internal Revenue laws; it has been a source of difficulty and confusion in the lower courts; it is a question which has not been but ought to be resolved by this Court.

A. The preferential tax treatment afforded to capital gains evidences, in its broadest terms, a Congressional purpose to differentiate between the gains realized on the conversion of a capital investment and the profits earned through the everyday conduct of a business. *Corn*

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buying and selling cotton to customers, he was not precluded from buying particular lots of cotton as an investment and selling such cotton as capital assets. The Court observed (p. 268) that a taxpayer has the right to engage in more than one business and that it was a question of fact whether the cotton was originally acquired as an investment. But where it was so acquired, as the jury had concluded, the Court held that the sale was not to customers in the ordinary course of the taxpayer's business even though, simultaneously, the taxpayer was engaged in that very same business with respect to other cotton. *Patterson v. Hightower*, 245 F. 2d 765 (C. A. 5th), is a similar holding.

The view of the Court below that property, originally acquired by a partnership as an investment, is sold in the ordinary course of a trade or business because some or all of the partners had previously or subsequently held a stock interest in corporations engaged in such a business, is also opposed to the many decisions holding that the business of a corporation is not the business of its stockholders. (See *Dalton v. Bowers*, 287 U. S. 404; *Burnet v. Clark*, 287 U. S. 410; *Deputy v. du Pont*, 308 U. S. 488.)

It will be observed that in *Curtis Company v. Commissioner*, 232 F. 2d 167 (C. A. 3rd); *Philber Equipment Corp. v. Commissioner*, 237 F. 2d 129 (C. A. 3rd), *Greenspon v. Commissioner*, 229 F. 2d 947 (C. A. 8th); and *Dillon v. Commissioner*, 213 F. 2d 218 (C. A. 8th), the taxpayers were either directly engaged in the identical trade or business, or had a stock interest in a corporation so engaged, but these Courts of Appeals rejected the conclusion that this meant that the taxpayers were engaged in a business while liquidating their investment property.

*Products Ref. Co. v. Commissioner,* 350 U. S. 46; *Burnet v. Harmel,* 287 U. S. 103. The latter is taxed at ordinary income tax rates under a progressive rate structure, and the former at a flat rate so as not to impede the sale or liquidation of capital investments. The statute, beginning with the adoption of special provision for the taxation of capital gains in the Revenue Act of 1921, has attempted to draw this distinction, and, by amendments from time to time, Congress has acted to fortify this objective by making explicit provision for capital gain taxation of some kinds of property and by excluding other kinds of property from the concept of what is a capital asset.

One of the most troublesome of these exclusions and the source of a large number of cases and considerable confusion in the lower courts, is the statutory exception relating to property held primarily for sale to customers in the ordinary course of a taxpayer's business. Where a capital asset is being sold, it is obviously being held primarily for sale (at least just prior to the sale) and, at that time, in the usual situation, it is being held primarily for sale to customers.[7]

If the statute contained no more, there would never be a situation where property which is sold could be treated as a capital asset. But the language "in the ordinary course of his trade or business" prevents the

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[7]The for sale "to customers" language and the word "ordinary" were added in Section 117(c) of the Revenue Act of 1934 to insure that this exception would not apply to a stock speculator trading on his own account and that he would be taxed with capital gain or loss on his security transactions. (H. Conf. Rep. No. 1385, 73d Cong., 2d Sess. (1939-1 Cum. Bull. (part 2), pp. 627, 632); *Farell v. Jarecki,* 231 F. 2d 281 (C. A. 7th), certiorari denied, 352 U. S. 830.)

statute from being self-defeating; thus, even though property (which is not otherwise excepted) is being held primarily for sale to customers, it will qualify as a capital asset unless it is being held for sale in the *ordinary course of a trade or business.*

There are, to be sure, many instances where the scope of the controversy centers on the question whether the property was acquired for the purpose of being resold in a trade or business. This presents, for the most part, a question of fact. Where, as here, property is acquired for *use*, rather than for *resale*, the crucial issue arises whether a later disposition of the property is sufficient to constitute a trade or business within the meaning of the statute where the taxpayer engages in no activity other than that reasonably suited to effectuate an expeditious liquidation of the property at the best possible prices. As we have seen, the Courts of Appeals for the Third, Seventh, and Eighth Circuits have held that such activities do not constitute a trade or business, while the Court below arrived at the opposite conclusion.

B. Other Courts of Appeals and, indeed, the Ninth Circuit itself, have evidenced difficulty in achieving a uniform interpretation and application of the statutory provisions, for decisions within a given circuit are frequently inharmonious or difficult to reconcile. Contrast, for example, the Tenth Circuit's reversal of the Tax Court in *Victory Housing No. 2, Inc. v. Commissioner*, 205 F. 2d 371, with its affirmance of the Tax Court in *Home Co. v. Commissioner*, 212 F. 2d 637; *Mauldin v. Commissioner*, 195 F. 2d 714; *Friend v. Commissioner*, 198 F. 2d 285. Contrast the decisions of the Fifth Circuit in *Ross v. Commissioner*, 227 F. 2d 265; *Consolidated Naval Stores Company v. Fahs*, 227 F. 2d 923; *Goldberg v. Commissioner*, 223 F. 2d 709; *Smith v. Commissioner*, 232 F. 2d

142; *Delsing v. United States*, 186 F. 2d 59; and *Fahs v. Crawford*, 161 F. 2d 315, with its decisions in cases like *Galena Oaks Corp. v. Scofield*, 218 F. 2d 217; and *King v. Commissioner*, 189 F. 2d 122. Compare the Fourth Circuit's decisions in *Camp v. Murray*, 226 F. 2d 931, with *Lakin v. Commissioner*, 249 F. 2d 781; and *Peebles v. Commissioner*, 249 F. 2d 92. Contrast the decisions of the Ninth Circuit in *McGah v. Commissioner*, 193 F. 2d 662 and 210 F. 2d 769, reversing the Tax Court, with decisions such as *Palos Verdes Corp. v. United States*, 201 F. 2d 256; *Rollingwood Corp. v. Commissioner*, 190 F. 2d 263; *Ehrman v. Commissioner*, 120 F. 2d 607 (C. A. 9th); *Commissioner v. Boeing*, 106 F. 2d 305, as well as with its decision in the present case.

The foregoing is a sampling and far from an exhaustive compilation of the decisions of these Courts of Appeals. In their totality they demonstrate that there is an urgent need for guidance, which this Court alone can furnish, respecting the basic principles to be applied in adjudicating this fundamental, frequently litigated issue.[8]

C. The issue concerning the proper meaning of 1939 Code Sections 117(a)(1)(A) and 117(j)(1)(B) is one of continuing importance for, as we have seen (*supra*, pp. 7-8), the statutory language has been continued in Sections 1221(1) and 1231(b)(1)(B) of the 1954 Code.

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[8]Professor Surrey has indicated the "great areas of uncertainty" which exist on this question and has noted how some of the cases "divide." Surrey, Definitional Problems in Capital Gains Taxation, 69 Harv. L. Rev. 985, 990, 991, fn. 12. Weithorn, Subdivisions of Real Estate—"Dealer" v. "Investor" Problem, 11 Tax L. Rev. 157, says: "The decisions . . . represent a confusing body of case law, not readily susceptible to logical analysis." See also Miller, The "Capital Asset" Concept: A Critique of Capital Gain Taxation, 59 Yale L. J., 837 and 1057.

The proliferation of litigation, which has been characteristic of these code sections in the past, will only be intensified in the future if the conflict between the Circuits, which has emerged with clarity only within the past several years, continues to exist. The resolution of this conflict is plainly a matter of importance and review by this Court is fully warranted.

## III.

## The Decision Below Is Erroneous.

The Congressional purpose in taxing capital gains at a preferential rate is to relieve taxpayers from "excessive tax burdens on gains resulting from a conversion of capital assets and to remove the deterrent effect of those burdens on such conversions." *Burnet v. Harmel*, 287 U. S. 103, 106. See also *Corn Products Ref. Co. v. Commissioner*, 350 U. S. 46, 52. At the present high level of surtax rates on ordinary income, the burdens on such conversions are even more onerous than when Congress first decided in the Revenue Act of 1921 to tax capital gains at a preferential rate, rather than to relieve them from tax altogether, as is true under the British system. At the same time, this Court has been sensitive to the policy of Congress that the profits arising from the "everyday operation of a business be considered as ordinary income." *Corn Products Ref. Co. v. Commissioner*, 350 U. S. 46, 52.

There is nothing to indicate that Congress intended that mere liquidation of capital assets should be regarded as a business or that it was more concerned with the deterrent effects of taxing, at ordinary income tax rates, the gains of the investor whose investment property is capable of being sold in its entirety to a single purchaser

than it was with the taxpayer who has invested in numerous pieces of property which, if they are to be disposed of so as to realize their full value, must be sold to numerous purchasers.

In the main, the criteria applied by the Court below as reasons for affirming the Tax Court add up to nothing more than that (*Curtis Company v. Commissioner*, 232 F. 2d 167, 170) "By the very nature of the case [the taxpayers] had to sell the properties a piece at a time." The selling activities of Boland, the real estate broker (which the Court below attributed, erroneously, we believe, to the taxpayers), signify no more than that the taxpayers (*Ross v. Commissioner*, 227 F. 2d 265, 268) "had a lot of houses to sell." If, as we believe (a view shared by three Courts of Appeals), Congress did not intend to tax the sale of an investment property in the same manner as the active conduct of a business, or to deter liquidation of large holdings, the Court below was clearly wrong in its conclusion.

We do not, of course, contend that an investor can never become engaged in a trade or business with what was once his investment property. A taxpayer may decide to enhance the value of his property for purposes of resale, imparting improvements to it by his personal efforts or through the efforts of others. Thus, a taxpayer may purchase a parcel of raw land to await an increment in value; but he may later change his purpose, subdivide the property and erect buildings for the purpose of selling them. In such a situation, the property has so changed its character as to be no longer identifiable as the original investment. The enhancement in value is attributable, not to an increment in the taxpayer's capital, but to the values imparted by the business on which the taxpayer

has embarked, *i.e.*, the erection and sale of improvements. Or, in some circumstances, a taxpayer may start a business by changing what was once investment property into, in effect, an opening inventory or stock in trade.

The present case, however, is not one of a taxpayer who sells, to buy again for resale. Here, there was a pure increment in the value of the taxpayers' capital. And here, the capital investment was sold to permit a more advantageous, new investment, the immediate proceeds of the liquidation being reinvested in other capital assets, principally in securities, but also in a building which the taxpayers continued to hold for rental purposes from 1948 until 1952 when it was disposed of in a forced sale under threat of foreclosure. [R. 210-213, 514.] In short, this is the typical case of a taxpayer who liquidates one investment in order to make another. It is the kind of situation which Congress did not seek to deter by the imposition of ordinary income tax rates.

## Conclusion.

In view of the foregoing, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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MITCHELL, SILBERBERG & KNUPP,
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March, 1958.

## APPENDIX.

### Opinion of the Court of Appeals for the Ninth Circuit.

United States Court of Appeals for the Ninth Circuit.

Edward Pool and Lottie Pool, Edward Pool, Lottie Pool, William K. Murphy, Edna Murphy, William K. Murphy and Edna Murphy, Petitioners, vs. Commissioner of Internal Revenue, Respondent. No. 15399. Dec. 18, 1957.

On petition to review decisions of the Tax Court of the United States.

Before: Lemmon and Barnes, Circuit Judges; Yankwich, District Judge.

YANKWICH, District Judge:

In this review of the determination of income tax deficiencies against the taxpayers for the calendar years 1946, 1947 and 1948, six consolidated cases are involved. The decisions of the Tax Court were entered on August 20, 1956. The deficiencies were as follows:

| | |
|---|---|
| For the years 1946-1947 Edward Pool | 5,697.02 |
| | 86,828.50 |
| For the years 1946-1947 Lottie Pool | 5,697.02 |
| | 86,828.50 |
| For the year 1948 Edward and Lottie Pool | 18,651.22 |
| For the years 1946-1947 William K. Murphy | 3,410.79 |
| | 98,401.48 |
| For the years 1946-1947 Edna Murphy | 3,410.79 |
| | 98,401.48 |
| For the year 1948 William K. and Edna Murphy | 17,349.60 |

It is the contention of the taxpayers that the decisions are clearly erroneous and should be set aside.[1] It is also argued that these are cases in which the Tax Court misapplied the law to proved facts.[2] In the main, it is asserted that the Tax Court erred in treating the income derived from the sales of two sets of duplexes owned by the petitioners as ordinary income under Section 22 of the Internal Revenue Code of 1939.[3] To the contrary, it is insisted that the sales should have been treated as the liquidation of an investment and the income subjected to the tax called for by the capital gain provision of Section 117(j) of the Internal Revenue Code of 1939.[4]

## I

## The Criteria Under 117(j)

Cases of this character present difficulties because there is no agreement among the courts as to what primary element in the transaction determines its character. In a recent case this Court, after enumerating some of the elements which the various Courts of Appeals have considered, at times determinative, states the conclusion that, in the last analysis, the question is one of fact:

> "What is and what is not trade or business and when property is or is not held for sale to customers are questions of fact.
>
> "Provisions similar to the one under discussion have been part of our tax statutes for many years. Courts

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[1] 26 U.S.C. 1952 Ed., § 1141(a) and (c); I. R. C., 1954, § 7482(a) and (c)(1); Rule 52(a), Federal Rules of Civil Procedure.

[2] McGah v. Commissioner, 9 Cir., 1954, 210 F. 2d 769, 771-772; Earle v. Woodlaw, 9 Cir., 1957, 245 F. 2d 119, 126-128.

[3] 26 U.S.C., 1952 Ed., § 22.

[4] 26 U.S.C., 1952 Ed., § 117(j)(a); Treasury Regulation 111, § 29.117-1.

have sought to evolve criteria by which to determine whether a person or an association was engaged in business. More particularly, they have tried to establish criteria by which to determine whether real property is held for investment or sale to customers in the ordinary course of business. Many tests have been proposed by this and other courts. Among them are: (1) the nature of the acquisition of the property, (2) frequency and continuity of sales over a period of time, (3) the nature and extent of the taxpayer's business, (4) the activity of the seller about the property, such as the extent of his improvements or his activity in promoting sales, (5) the extent and substantiality of the transaction and the like. * * * But in the last analysis, each case must be determined upon its own specific facts, for none of these incidences are present in all cases."[5]

Cases, old and new, in this Circuit have, at times, emphasized one or another of these criteria. Thus, in a case preceding the one just cited, this Court said:

"We have heretofore decided that a mere series of sales for the primary purpose of liquidation does not

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[5]Stockton Harbor Industrial Co. v. Commissioner, 9 Cir., 1954, 216 F. 2d 638, 650. In another case the factors to be taken into consideration are stated to be:

". . . the frequency and continuity of sales; the purpose for which the property was originally built; whether there was a bona fide change from the original purpose of building houses for sale; the extent and substantiality of the sales income as compared to the rental income earned by the company. These are factors commonly considered by other courts in making such a determination. See Victory Housing No. 2 v. Commissioner, 10 Cir., 1953, 205 F. 2d 371; Mauldin v. Commissioner, 195 F. 2d 714, *supra*; Commissioner of Internal Revenue v. Boeing, 106 F. 2d 305, *supra*. None of the factors stated above was cited as being controlling but all were considered by the Tax Court. (Cohn v. Commissioner, 9 Cir., 1955, 226 F. 2d 22, 24.)"

solve the problem. Ehrman v. Commissioner, supra. The holder may well have acquired and held the property for an ordinary turnover profit and found that it could not be sold for a reasonable price without submitting it to conditions prevalent to a trade or business. In such *case the owner has changed the status of his holding, whether or not it was contrary to his first desire."*[6] (Emphasis added.)

This and other courts have stated repeatedly that "there is no fixed formula or rule of thumb"[7] for determining whether property is held primarily for sale to customers in

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[6]Palos Verdes Corp. v. United States, 9 Cir., 1952, 201 F. 2d 256, 258-259. As stated in Rollingwood Corp. v. Commissioner, 9 Cir., 1951, 190 F. 2d 263, 266:

"While the purpose for which the property was acquired is of some weight *the ultimate question is the purpose for which the property is held.*" (Emphasis added.) The line of cases in which this Court has refused to consider liquidation, either directly or through agents, as determinative of the matter, is unbroken: Richards v. Commissioner, 9 Cir., 1936, 81 F. 2d 369, 372-373; Commissioner v. Boeing, 9 Cir., 1939, 106 F. 2d 305, 309; Ehrman v. Commissioner, 9 Cir., 1941, 120 F. 2d 607, 610; Rollingwood Corp. v. Commissioner, 9 Cir., 1951, 190 F. 2d 263, 266; Cohn v. Commissioner, 9 Cir., 1955, 226 F. 2d 24; Achong v. Commissioner, 9 Cir., 1957, 246 F. 2d 445, 447. In the light of this, the seemingly contrary conclusion reached by the Court of Appeals for the Third Circuit in Curtis Company v. Commissioner, 1956, 232 F. 2d 167, loses significance. The strong dissent by Circuit Judge McLaughlin stresses the fact that the majority opinion is contrary to the decisions of this court Richards v. Commissioner, *supra;* Rollingwood v. Commissioner, *supra;* and Cohn v. Commissioner, *supra,* are cited as stating the correct principle that "the manner and purpose of holding property may change or be twofold" (p. 172). And this Court in Achong v. Commissioner, *supra,* distinguishes the Curtis case because "the sales were of homes previously owned for rental without any change to facilitate sale." (P. 447.)

[7]Mauldin v. Commissioner, 10 Cir., 1952, 195 F. 2d 714, 716; Cohn v. Commissioner, 9 Cir., 1955, 226 F. 2d 22, 24; Pacific Homes v. United States, 9 Cir., 1956, 230 F. 2d 755, 759.

the ordinary course of the taxpayer's business. The reason is that the problem usually arises in

> "situations where the taxpayer is engaged in some activity apart from his usual occupation and the question is whether this activity amounts to a business."[8]

Even the management of one's own property may or may not be "a business" depending on circumstances.[9] And in dealing with the sale of lands the applicable rule has been well summed up by the Court of Appeals for the Fifth Circuit:

> "An occasional sale of land held as an investment is not such a business though profit results. The word, notwithstanding disguise in spelling and pronunciation, means busyness; it implies that one is kept more or less busy, that the activity is an occupation. It need not be one's sole occupation, nor take all his time. It may be only seasonal, and not active the year round. It ordinarily is implied that one's own attention and effort are involved, but the maxim qui facit per alium facit per se applies, and one may carry on a business through agents whom he supervises."[10]

And Courts of Appeals, including this one, have warned that, in the end, the decision in each case must depend upon the particular facts in the case.[11] The Court of Appeals

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[8]Rollingwood Corp. v. Commissioner, *supra*, Note 6, p. 266.

[9]Higgins v. Commissioner, 1941, 312 U.S. 212, 218. See, Lykes v. Commissioner, 1951, 343 U.S. 118, 121-122, for legislative change as to deductibility of certain expenditures since the decision was made. The concept of what is business is not changed.

[10]Snell v. Commissioner, 5 Cir., 1938, 97 F. 2d 891, 892.

[11]See cases cited in Note 7.

for the Tenth Circuit expressing itself in accord with this view has stated:

> "Neither is it possible in the resolution of these questions to adopt fixed indices from which the answer can be reached. There are, however, certain factors which have been recognized as helpful guides in seeking a just and correct result. Among these are the purposes for which the property was acquired, the activities of the taxpayer and his agents with respect thereto such as making improvements on the property, conducting a sales campaign either through advertisements or the employment of real estate agents, the frequency and continuity of sales as differentiated from isolated sales, as well as any other factor reasonably tending to show that the transaction was in furtherance of or in the course of the taxpayer's occupation or business."[12]

These warnings are significant because the taxpayers in this case would have us abandon the flexible formulas which Courts have established in favor of a rigid formula that *"would fit"* the variety of cases which have arisen. Thus, they would place in one group cases in which the original intention is obscure.[13] In another group they would include cases in which the character of the property was changed.[14] In the third group they would gather cases where there is an original investment purpose and

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[12]Home Company v. Commissioner, 10 Cir., 1954, 212 F. 2d 637, 639. And see, Mauldin v. Commissioner, *supra*, Note 7.

[13]Rollingwood v. Commissioner, *supra*, Note 6; Cohn v. Commissioner, *supra*, Note 6; Homann v. Commissioner, 9 Cir., 1956, 230 F. 2d 671.

[14]Commissioner v. Boeing, *supra*, Note 6; Richards v. Commissioner, *supra*, Note 6; Erhman v. Commissioner, *supra*, Note 6.

a later decision to sell.[15] The taxpayers urge that the present case is in the latter group and that the Tax Court erred in not so ruling.

It is not necessary for us to determine the validity of the rigorous distinctions which the taxpayers have sought to introduce into the cases which have dealt with the problem. What they have done is the very thing against which this and other courts have warned. They have taken one or another of the criteria which have been resorted to and sought to *enshrine it as a rigid category*. The teachings of the cases is that this cannot and should not be done. The excellence of our jurisprudence is its flexibility. In applying general statutory language to particular situations, courts best conform to the tradition of growth of our system when they adapt realistically general principles to different or constantly changing situations. In applying tax statutes, the best result is always achieved when we avoid harsh crystallizations.

## II

### The Undisputed Facts in the Case.

If we apply the criteria referred to above[16] to the situation before us, we cannot say that the decision of the Tax Court was clearly erroneous.[17] Nor are we convinced that the Tax Court applied the wrong principles of law to admitted facts.[18]

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[15]Chandler v. United States, 7 Cir., 1955, 226 F. 2d 403; Curtis Co. v. Commissioner, 3 Cir., 1956, 232 F. 2d 167, which is commented on in Note 6; Victory Housing No. 2 v. Commissioner, 10 Cir., 1953, 205 F. 2d 371.

[16]Stockton Harbor Industrial Co. v. Commissioner, *supra*, Note 5; Pacific Homes v. United States, *supra*, Note 7.

[17]See references in Note 1.

[18]See reference in Note 2.

*1. Stipulated Facts.*

In determining the matter it is necessary to go, with some detail, into the background out of which the controversy arises. Many of the facts were not disputed. In outline, the following facts were stipulated. They are given (with some omissions and changes of language) in the form in which they appear in the stipulations.

Edward Pool and Lottie Pool are husband and wife. At all times herein material, they filed their federal income tax returns on a cash and calendar year basis with the Collector of Internal Revenue for the Sixth District of California. Separate returns were filed for the years 1946 and 1947 but joint returns were filed for the year 1948.

William K. and Edna Murphy are husband and wife. At all times herein material, they filed their returns on a cash and calendar year basis with the Collector of Internal Revenue for the Sixth District of California. In 1946 and 1947 each filed separate returns. In 1948, however, they filed joint returns.

Artcraft Builders, Inc. (hereinafter referred to as "Artcraft") is a California corporation. Until 1944 its principal place of business was at Los Angeles, California. Since 1945 its principal place of business has been at Long Beach, California.

Artcraft was organized as a California corporation on March 10, 1941. Four thousand shares of Class A preferred stock and 21,000 shares of Class B Common stock were authorized. Class A and Class B stock were entitled to equal voting rights, share for share. The Class A shares carried the right to cumulative dividends at the rate of 8 per cent.

On incorporation, 800 of the Class A shares were issued to R. T. Cooke and Mary Cooke and the remaining 3,200

shares were issued to J. S. A. Smith and Gertrude C. Smith. The Class B shares were issued as follows: 200 shares to R. T. & Mary Cooke; 800 shares to J. S. A. and Gertrude C. Smith; 1,000 shares to Edward Pool; 1,000 shares to William K. Murphy.

In April, 1943, an additional 25,000 shares of Class B stock were authorized and issued as follows: Edward Pool, 8,400; William K. Murphy, 8,300; J. S. A. Smith, 6,600; R. T. Cooke, 1,700.

On or about June 1, 1943, William K. Murphy and Edward Pool and their wives purchased all the stock held by Mr. and Mrs. J. S. A. Smith and Mr. and Mrs. R. T. Cooke. On June 8, 1943, Smith and Cooke resigned as officers and directors of Artcraft.

At all times thereafter the Pools and the Murphys have been the sole stockholders of Artcraft. From that date the Pools have owned 14,050 shares of the Class B stock as community property and the Murphys have owned 13,950 shares of Class B stock as community property. Each couple has from that time owned 2,000 shares of Class A stock as community property. The Pools paid a total of $16,000.00 for all their stock in Artcraft and the Murphys paid a total of $16,000.00 for theirs.

In 1941, Artcraft constructed houses under individual building contracts for others. In 1942, Artcraft had some income from contracts with outsiders, but the major portion of its income was derived from building houses for sale on its own account. In 1942, Artcraft built for sale on its own account and sold 142 houses in Tract No. 12951, Los Angeles County. In 1943, Artcraft built for sale on its own account and sold 2 houses in Tract 12951, 86 houses in Tract 12287, and 100 houses in Tract 12288, all tracts being located in Los Angeles County, California.

No income was derived by Artcraft in 1943 from building on contracts for others.

On May 26, 1943, Artcraft made application with the Federal Housing Administration and the War Production Board for approval to build 70 duplexes (containing 140 units) in Tract 11451. This application was approved by the Federal Housing Administration on June 7, 1943, and by the War Production Board on June 16, 1943. After construction, deeds to Lots 1 to 70, inclusive, of Tract 11451, with improvements, were executed by Artcraft and delivered on or about March 31, 1944, to Edward Pool, Lottie Pool, William K. Murphy and Edna M. Murphy, as tenants in common, the grantees acquiring an undivided, one-fourth interest each. One hundred duplexes were constructed in Tract 13163, and deeds to Lots 1 to 100, inclusive, of that Tract, with improvements, were executed by Artcraft, bearing date of March 21, 1946, to W. K. Murphy, Edna Murphy, Edward Pool and Lottie Pool, as tenants in common, with grantees acquiring an undivided one-fourth interest each. The lots in these tracts, with improvements, were transferred to the four stockholders of Artcraft at cost to the corporation.

The four individuals, Edward Pool, Lottie Pool, William K. Murphy and Edna Murphy, on or about April 1, 1944, formed a joint venture (or partnership) known as "Edward Pool and Associates" (hereafter referred to as "Associates"). Thereafter Associates kept its books on the accrual method and fiscal year basis ending January 31 of each year.

Both groups, Tracts 11451 and 13163, of units were rented after completion. Artcraft performed the role of rental agent for Associates for the period Associates owned the properties referred to. As such rental agent

Artcraft entered into leases, collected rents, kept books, paid bills and generally managed the property.

All dwelling units here involved were subject to rent control during the taxable years. Permission was obtained for rentals charged from the proper governmental agency.

*2. Wartime Restrictions. Priority Assisted Housing.*

A proper understanding of the facts requires a brief summary of the wartime restrictions on housing and the requirements for approval by the Federal Housing Administration and by the War Production Board referred to in the stipulations.

General Orders 60-2 and 60-3 were part of the Operating Manual, National Housing Agency. General Order No. 60-2 was designated as "Public Regulations—Occupancy and Disposition of Private War Housing," while General Order No. 60-3 was designated as "Public Regulations—Methods of Disposition of Private War Housing Including Rent Levels, Sales Prices, and Petitions to the National Housing Agency."

General Order 60-2 recited that the National Housing Agency was responsible for the proper occupancy of housing programmed for war workers and for the adoption of regulations assuring that war housing would be available for eligible war workers for the duration of the national emergency declared by the President on September 8, 1939. Under it, private war housing was to be regarded as "begun" on the date of submitting to the Federal Housing Administration a properly executed application for priority assistance or authority to begin construction in connection with such housing, and the date of "completion" was to be the date upon which such housing was offered

for initial rental or sale, or the date upon which it was first ready for immediate occupancy, whichever was later. The phrase "held for rental" was defined to include "only an ordinary landlord-tenant relationship or such a tenancy coupled with an option to purchase." Under the option, the tenant was not to be obligated to purchase and the option was to run only in his behalf. The selling price was to "be a fair market price, or $6,000," whichever was lower. The option to purchase could not be exercised prior to the expiration of four months' occupancy, and was to continue for at least 30 months, unless sooner exercised. Private war housing begun on or after February 10, 1943, was to be made available for initial occupancy, and for reoccupancy, only by eligible war workers. It was provided, however, that at any time subsequent to 60 days after completion of such housing, the owner might petition the National Housing Agency to permit initial occupancy, or reoccupancy, as the case might be, by a person other than an eligible war worker. Except for involuntary transfers, private war housing could be disposed of (a) only to an occupant, after 4 months' occupancy; (b) to a person who would not himself occupy the housing, provided the occupancy and disposition limitations applicable prior to purchase or acquisition should continue to be applicable after such purchase or acquisition; or (c) at any time subsequent to 60 days after completion of any such housing, the owner might petition the National Housing Agency to permit disposition otherwise than as indicated in (a) and (b).

General Order 60-3 was intended to implement the occupancy and disposition policies of the National Housing Agency applicable to all private war housing as stated in General Order No. 60-2. It also provided that for the duration of the national emergency declared by the Presi-

dent on September 8, 1939, all private war housing begun on or after February 10, 1943, should be held for rental to eligible war workers as provided in General Order 60-2, at the rentals specified in the application, which rentals should in no event exceed $50 per month shelter rent for one unfurnished dwelling unit, plus a reasonable charge for tenant services, which was not to exceed $3 per month per room. It also embodied a provision that "a dwelling unit * * * may be purchased by an occupant (initial occupant or reoccupant) after four months of continuous occupancy." But that the purchase price could not exceed the fair market price, or $6,000, whichever was lower. In the case of such sale, the seller was required to submit an agreement on the part of the purchaser that such purchaser would continue to occupy the dwelling unit, or would hold the unit subject to the occupancy and disposition provisions set forth in General Order No. 60-2. Subject to the same restrictions as to price, such houses could also be transferred to a person who would not become an occupant thereof, but only if an agreement was submitted stating that the housing would be held subject to the provisions of General Order No. 60-2. At any time subsequent to 60 days after completion, the original owner or a subsequent owner could petition the National Housing Agency to permit disposition otherwise than as provided in the regulation.

General Order No. 60-3 was later superseded by General Orders Nos. 60-3A, 60-3B, which became effective August 25, 1943, and 60-3C, which became effective November 12, 1943. The superseding orders were, for the purpose of the question before us, substantially the same as General Orders Nos. 60-2 and 60-3.

## III

### The Facts Found.

*1. The Business of the Taxpayers.*

The preceding facts are, in the main, admitted. The dispute arises in evaluating the facts testified to by the taxpayers and the inference which the Tax Court drew from them and the mass of written data. After conceding that an intention to hold for rental may have existed for a time, the Tax Court stated as its final opinion

> "that the duplexes on Tracts 11451 and 13163 were held by the petitioners primarily for sale to customers in the ordinary course of their business and that they were sold to customers in the ordinary course of that business."

A specific finding to this effect was also made.

If we apply the tests already given[19] it is quite evident to us that, regardless of any original avowed intention to build the particular projects for rental purposes, the business of the taxpayers which they conducted, either directly or through various corporations, which they dominated, of which these transactions were a part, was building for sale and profit. Murphy had been associated with various corporations engaged in building, finance and manufacturing. When he came to California in 1934 he outlined for a finance and construction company plans of apartment buildings and home lay-outs. Later on, in 1941, he, J. S. A. Smith, Edward Pool and Artie Cooke and their wives organized Artcraft to build apartment buildings and homes for individuals on contract. In 1941 they began to interest themselves in wartime priority assisted housing. They

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[19]See cases cited in Notes 5, 6 and 7.

applied for and received permission to build the particular structures subject to restrictions as to rental and resale price. The stipulation of facts states that before building the units here involved they built for sale through Artcraft in 1942, 142 houses and 188 in 1943 in tracts which they owned.

While testifying that both he and Pool intended to retain the units here involved for definite income Murphy also stated that their attorneys advised them to discontinue the policy of giving yearly leases on the premises. The last lease was made in April 1946. As leases expired they were not renewed. Murphy admitted that after failing to secure rental increases in 1945 he began to listen to the suggestion of his accountant that the properties be sold because they had risen in value and a large profit could be realized. In the course of his interrogation and while discussing the agreement with Mr. Philip Boland, to act as sales broker, a very significant phrase came in. The phrase: "speculative builders." The record reads:

> "Q. Do you know whether it is customary for a *speculative builder* to pay a straight five per cent commission to an independent broker or is it customary to do something else?
>
> A. Well, a speculative builder usually agrees on so much a building, like we paid, I think, for houses, either 50 or a hundred. They agree on a price. They don't usually pay any five per cent, no." (Emphasis added.)

Edward Pool had been a contractor all his life and he characterized his activities as "speculative builder." At

the trial the following colloquy occurred between Pool and counsel for the Government:

"Q. Were you a builder of houses for sale on your own account? I mean, did you build the houses and then have them sold?

A. It was contracted, mostly, and then they could, as you say, you go out and spec on a half-dozen good lots.

The Court: What do you mean, 'spec'?

The Witness. When you build them and they are not contracted for previously, you know, until you finish them, and then you sell them on the market to people who come along and buy them.

Q. (By Mr. Axelrad). In other words, you build them yourself and sell them, and you made the profit on them yourself?

A. Yes, sir.

Q. How much of that did you do?

A. Not so much. In other words, when we moved to Long Beach, we built a few homes, you know what I mean, in tracts and built them and sold them as we built them. *They were speculative.* They were not contracted for prior to starting.

Q. You are talking about Artcraft now, are you?

A. Yes, sir.

Q. I am talking about your own private enterprises prior to Artcraft. You said you were a builder all your life.

A. That's right.

Q. What do you mean by that?

A. *I built residential properties all my life, individual homes and rental units.*

Q. *Did you sell them and make a profit on what you sold?*

A. *Yes.*

Q. Or did you build them on contracts for others?

A. Both. *The only time I would build for the market, as we say, speculatively, is when you would happen to hit a half-dozen or a dozen real good lots, good locations.*" (Emphasis added.)

In the law of taxation, the courts have recognized the distinction between a person who buys securities (or other property) as a long term investment and the one who buys them for speculative purposes in expectation of a rise in the market and for resale to any buyer for a profit.[20]

While the money derived from the sale of these properties was invested by Murphy and Pool in stocks, within two years, they organized corporations in Colorado and New Mexico with the same name as their California building firm (Artcraft Builders), the purpose of which was the building and disposition of residential property for profit. From the Colorado corporation Murphy received

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[20]Schafer v. Helvering, 1936, 299 U.S. 171, 174. The Court of Appeals for the Fourth Circuit, after approving the rulings of this Court in Richards v. Commissioner, *supra*, Note 6, and in Welch v. Solomon, 9 Cir., 1938, 99 F. 2d 41, states the distinction in this manner:

"A distinction has been drawn between investors and speculators who trade in securities on their own account and dealers who keep a supply of securities on hand for resale to customers. But in these cases even under the earlier form of the statute, the significance of a resale to customers was recognized when the courts came to inquire whether a particular taxpayer was an investor or speculator on the one hand or a dealer on the other." (Gruver v. Commissioner of Internal Revenue, 4 Cir., 1944, 142 F. 2d 363, 368.)

While these expressions are used in conjunction with persons dealing in securities, there is no valid reason for not applying them to those who deal in improved real property. They, too, can buy for long-term "investment" or for "speculation" and quick turn-over.

a salary of $750 a week as the secretary and treasurer in charge of financing and Pool the same salary as the builder. They drew $500.00 a week each from the New Mexico corporation for like duties. So, considering the particular venture in relation to the general activities of the two partners—their "busyness"—we may well apply to their activities before and after the words of the Court of Appeals for the Fifth Circuit in another case:

> "It seems fairly inferable from the record that at all times he had (houses) for sale, and that the volume sold depended primarily upon the prevailing economic conditions brought on by wartime activities and their aftermath."[21] (The word "houses" is substituted for "lots.")

While the wartime restrictions on resale of wartime and priority assisted housing continued and until they were

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[21]Mauldin v. Commissioner, 10 Cir., 1952, 195 F. 2d 714, 717. McGah v. Commissioner, 9 Cir., 1954, 210 F. 2d 769, does not go counter to this conclusion. There the taxpayers were forced to sell because a bank

> ". . . became concerned about the large debt owed by petitioners and demanded that they liquidate some of their properties in order to reduce their indebtedness. It was under this compulsion that the petitioners decided to sell some of the houses then held for rental purposes." (P. 771.)

Here, the taxpayers acted *under no compulsion*. They merely decided to sell when the opportunity for high profits presented itself and when they were satisfied, at least in Murphy's case, that taxwise they would gain in that he had been advised that the increased profit would be treated as "capital gain". Much is made in the argument of the fact that Pool was not anxious to sell. However whatever reluctance he had was finally overcome. To some extent, Murphy may have been the dominant partner, as he was the financier of the group. However, the Tax Court was right in attributing to the partnership the acts of either. After all, in the law of partnership or joint venture, one partner, in carrying on the partnership business, may bind the other by his acts and even by his torts. See, Cal. Corp. Code, §§ 15009(1), 15013, Cal. Code of Civ. Procedure,

relaxed and finally removed on October 15, 1945,[22] it was not profitable to sell. The market was very restricted. The highest sales price was $6,000. As soon as the restrictions as to resale price were removed, the intention of Associates to sell was formed and their sale was achieved as quickly as possible. The opportunity then arose for an easy profit. Of the 70 duplexes in Tract 11451, 65 were sold at $11,800 per building and 6 at $12,000 per building. The 100 duplexes in Tract 13163 were sold at $13,000 per unit. The results were the unusually large profits from which this litigation stems. So that if it be conceded that the original intention was to hold the units for rental, that purpose was abandoned when a seller's market developed. In quick succession the first group was sold in a matter of a few weeks and the next group followed. So, in view of the prior activities of the taxpayers as builders of houses for sale at a profit, the sales under consideration partook of the nature of a business rather than liquidation.[23] It was a continuation of "speculative" selling, tem-

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§ 1870(5); B. F. Goodrich v. Naples, 1954, D.C. Cal., 121 F. Supp. 345, 353. Nor is the ruling in Victory Housing No. 2 v. Commissioner, 10 Cir., 1953, 205 F. 2d 371, controlling here. The Court there found that the taxpayer "neither bought nor developed real estate for sale". (P. 373.) The taxpayers here did. In that case, the taxpayer "did not advertise the houses for sale either through publication or by signs erected on the premises". (P. 373.) Here, the taxpayers did both, as the analysis of the sale and advertising campaign carried on indicates.

[22]The Executive Orders are found at 50 U.S.C. App. § 601, Supplement IV (1941-1945) (Executive Order 9070). The corresponding regulations are found in Code of Federal Regulations, Book 1, Title 24, Supplement 1943, Part 600, and in Book 2, Supplement 1944, to Code of Federal Regulations, Title 24, Parts 702-703. (General Orders 60-2 and 60-3 conformed to Parts 702-703 of this edition.) The final revision and revocation of private war housing regulations are found in Book 3, 1945 Supplement to Code of Federal Regulations, Title 24, Parts 702-703, pp. 2552 *et seq.*

[23]Home Company, Inc. v. Commissioner, 10 Cir., 1954, 212 F. 2d 637, 641.

porarily interrupted by war conditions. As stated by the Court of Appeals for the Fifth Circuit:

> "Congress intended to alleviate the burden on a taxpayer whose *property has increased in value over a long period of time.* When, however, such a taxpayer endeavors still further to increase his profits *by engaging in a business separable from his investment,* it is not unfair that his gain should be taxed as ordinary income."[24]

*2. The Method of Selling.*

One of the tests uniformly applied in all these cases is the frequency and continuity of the sales.[25] There is no question that once the sale was begun it was continued until both Tracts 11451 and 13163 were fully disposed of. The first deposit on the group of 70 was taken on May 4, 1946. Approximately ten weeks elapsed between the first and last sale. The first sale was closed on June 22, 1946, the last one on September 6, 1946, the sale being closed in October. This group of duplexes was sold to individual owners.

The selling of the second group, the one hundred group, occupied the remainder of 1946, and was completed by the end of July, 1947. This group of dupiexes was sold to two owners.

In the disposition of the property the activities of Philip P. Boland become important. Boland had been a real estate broker in California since 1939, except during the four years from 1942 to 1946 when he served in the armed forces. Upon taking terminal leave on January 3, 1946, he visited various persons, among them Murphy and Pool.

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[24]Galena Oaks Corp. v. Scofield, 5 Cir., 1954, 218 F. 2d 217, 220.

[25]See references in Note 5.

He approached them about selling the buildings which they had constructed during the war. At first they were not interested. Boland went back to Missouri to visit his relatives. Upon returning in April he again approached them about selling the property. In the meantime, he had become associated with Everett Davis & Son, brokers in Pasadena. As there was little property to sell he undertook to secure listings. On approaching Murphy and Pool he found Murphy receptive to the idea of selling but Pool was not agreeable. He tried to convince him that

> "the time was ripe for selling and they would never have as good opportunity to get rid of them again, that now was the best time to cash in on them."

As he put it, Murphy "saw it (his) way" and later Pool agreed to go ahead and sell some of the units. They agreed to allow him to sell the 70 units which they considered "the less desirable of their income property."

Boland agreed to accept, instead of the customary 5% commission, a fee of $500 a house and permission to use their office, telephone and whatever facilities were available to him in making the sale. He prepared the advertisements which bore the legend "Artcraft Builders, Inc." and their Long Beach address and also the legend that the property was being sold by the original builders. Very significantly he explained the advantage for using the name of Artcraft in this manner:

> "Q. And how did Artcraft's name get into the advertisement?
>
> A. Well, it was a matter of orientation. The property was known as the Artcraft Manor, and these mats, the signature mats, the newspapers had them, and it was a question of utilizing to the best advantage any tool that was available to sell the property.

Q. Did you consider that there was anything dishonest about saying Artcraft was selling something when you knew it wasn't?

A. No, not at all.

Q. Why not?

A. It was merely a matter of advertising. There was nothing unusual about it."

Boland employed two salesmen to assist him. Part of the time he had a girl in the office in addition to the help furnished him by Mrs. Ruby Jean Woodruff who was Artcraft's and Associates' secretary. He prepared the escrow instructions, paid for the advertising which did not exceed $2,500. He received a total of $35,000 for selling the houses in the first group. Later he arranged to sell the second group of 100 duplexes. All these sales were fully financed. The Bank of America having refused to finance the loans because the 100 duplexes were sold to two buyers together Murphy arranged with the Insurance Fund Mortgage Company of Massachusetts and Western Federal Savings and Loan Association to secure the financing.

The sale of the second group extended over a year. The sales were made from the office of Artcraft and Associates, the broker using their facilities. In addition to the advertising which bore the name of Artcraft, there is evidence in the record that, at times, communications to prospective buyers were issued under Artcraft's name. The fact that offices in the neighborhood were difficult to secure, as were also telephones, does not minimize these facts. Indeed, Boland and Murphy admitted that the reduction of the commission to a flat fee of $500 was in exchange for the use of these facilities.

While Boland states that, at times, Murphy gave him advice which was not of any value, the fact also remains

that the important matter of financing was arranged by Murphy. The advertisements stress sales not by the agent but by "the builders," the taxpayers' wholly owned building company. One such advertisement read:

FOR SALE
10 Duplexes
By the Builders
Immediate Possession
Two 5-Rm. Apartments
in Each
ALMOST NEW
Hardwood floors, tile bath and wainscoting. Pullman lavatory . . . one apartment vacant in each building . . . ready for purchaser to move in immediately at close of sale. Rent of one apartment will carry payments on the building. A splendid bargain either as a home or investment. Close to super-market drug store and shopping center.
PRICE $11,800
DOWN-PAYMENT
Approx. $720
(For Veterans)
$4650 for Non-Veterans
Open for inspection
Daily and Sunday Until 9 P.M.
ARTCRAFT BUILDERS, INC.
2187 LAKEWOOD BLVD.
LONG BEACH
(One Block North of Traffic Circle)
(West side of Lakewood Blvd.)
(Los Angeles Herald-Express, May 4, 1946)

On the whole, twenty such advertisements appeared in three Los Angeles newspapers, the Los Angeles Herald Express, Los Angeles Examiner, and Los Angeles Times. The earliest is dated May 4, 1946, which marked the beginning of the campaign to sell. The latest is dated November 17, 1946. All were substantially the same. In all the name Artcraft appeared. The emphasis was that the sale was "by the builders." Two advertisements bore the legend *"We're selling 27 duplexes."* At the bottom of the advertisements was the name "Artcraft Builders, Inc." One appeared in the Los Angeles Herald-Express on August 31, 1946, the other in the Los Angeles Examiner of September 1, 1946. Nowhere in any of these advertisements did the name of Boland appear as selling agent or broker.

Indicative of the fact that these were concerted sales on a seller's market is the nature of the advertisements. When the first advertisement for the group of seventy, which sold for $11,800, was written, it bore the legend "No down payment for veterans." As the sales went faster than predicted, the later advertisements were changed to indicate "down payments for veterans approximately $720.00, Non-veterans approximately $4,650.00."

As to the second group of one hundred, which sold for $13,000, a different procedure was adopted. The advertisements carried the following legend: "Down payment for veterans $2500. No down payment for 2 veterans. Down payment for non-veterans $6500." In all the service-man feature was emphasized. For most of the advertisements bore the legend "Quick service for veterans," and the statement that the properties were "fully approved to meet all GI appraisal and loan qualifications."

When dealing with persons with the business acumen of Murphy and Pool, denial by them of the knowledge of these advertising activities and the fact that the sales were being held out to the public as sales by Artcraft, their wholly owned building company, did not deserve being taken by the Tax Court at face value. So the Tax Court was justified in finding that the sales by Boland were sales by the taxpayers.[26] Boland was quick to resent any intimation that representation of sale by Artcraft implied any element of deception as the quotation from his testimony, already given, indicates. Indeed, he claims approval of the use of Artcraft's name in the sale from a deputy Real Estate Commissioner of California. And it may be assumed that Pool and Murphy would have resented any representation which did not conform to the facts. The fact that they did not indicates that the sales were indeed by them, under their auspices, at their office, under advertisements which stressed sale by builders with assistance in the financing as to the second group of units sold to two owners when that became important.

There are other facts that show the active participation of the taxpayers in the conduct of the sales. On the escrow instructions to the bank the names of the taxpayers were typed in advance of need. Under them was the word "By" and the testimony in the record is that one of the taxpayers wrote in his name, when a deal was made. Because some of these escrow instructions were prepared in

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[26]The Tax Court found:

"Beginning with the employment of Boland, the four individual petitioners herein began a business of selling real estate, and from April, 1946, the 70 duplexes on Tract 11451, and from July, 1946, the 100 duplexes on Tract 13163 were held by them primarily for sale to customers in the ordinary course of that business."

advance, there was a time lag between the date on their face and the signature. Illustrative is an escrow instruction dated August 20, 1946, on which the signing date is given as September 23, 1946. The testimony was that the date was typed in by the bank after the copy of the escrow was returned to the files of the taxpayers.

There are copies of correspondence in the record relating to changes of ownership, giving instructions as to financing and the like, bearing the legend: "Artcraft Builders, Inc., By"; Boland's name did not appear on any sign in the windows of the Artcraft Office, which was also the office of Associates. In the handling of the actual transfer of title, the procedure was this: The deeds to the property were signed in blank by the taxpayers and their wives and delivered to Mrs. Ruby J. Woodruff without the name of a buyer. A printed form of acknowledgment with the name of Mrs. Woodruff as notary was attached to each Grant Deed. When a buyer was secured, Mrs. Woodruff notarized the deed. So, at times, weeks passed between the time the deeds were signed by the taxpayers and the time they were completed with the name of a buyer and notarized. There is one exhibit in which the deposit receipt was dated August 18, 1946 and the deed presumably dated September 23, 1946. As this is an original, no acknowledgment appears. And one would gather from the correspondence that a sale to another than the person named as grantee may have been made. The escrow statements by the bank, on completion of each transaction were made to William Murphy et al.

All these factors converge to one point: In dealing with the public through advertisements, in the various formal documents relating to the transaction beginning with the escrow instructions to the final deeds, the name of Boland

as selling agent *did not* appear. The correspondence with the prospective buyer seems to have been carried on mainly in the name of Artcraft.

In the formal receipts which appear to be a printed form of the type in use in California for such purpose, the word "broker" appears in print as do also the words "seller" and "buyer." Such receipts, when deposits were made were signed by Boland. However, in carbon copies of letters, the original of which was signed by Boland, no indication as to his status as "broker" or "agent" appears under his signature—just the type name "Philip Boland." The money paid as a deposit was deposited in the bank in the name of the Associates.

There is another significant fact: Despite the magnitude of the transaction, no formal written contract relating to the sale of either group of duplexes was entered into with Boland. In his testimony, Boland stated that he put down his proposal as to the sale of the first group of seventy duplexes

> "in a letter and received back a letter more or less as a receipt of what I had sent, and eventually, why, they gave me the go-ahead sign, that they would sell 70 of them, the first 70 that had been built."

Neither letter is in the record. However, Mrs. Woodruff testified that a letter was dictated to her written to Boland with "a reference to selling the 70 duplexes and giving him authority or the exclusive or whatever it is called, to sell the 70 duplexes." As to the sale of the second group of 100 duplexes, there is no evidence of even this type of informal agreement.

So the conclusion is warranted that these sales were sales made primarily by, and in behalf of the taxpayers, with the broker paying part of the expense of the sales out of his commission.

## Summary and Conclusion

The record in this case is very extensive. The printed record alone, excluding the exhibits, covers 533 pages. The original transcript and exhibits sent up with the appeals run into hundreds of pages of typewritten and printed documents. All these (which we have studied), the Tax Court had before it. On them it based the one ultimate fact, important on this review, namely, that the duplexes sold during the taxable years were held primarily for sale to customers in the ordinary course of the taxpayers' business and that they were sold to customers in the ordinary course of that business. In a review of this character, our function is not to substitute our judgment for that of the Tax Court. Rather are we to determine if there is substantial evidence to support the conclusion reached by the Tax Court.[27] The trier of fact may disregard uncontradicted testimony, if it is improbable. What

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[27]"The trial judge has the function of finding the facts, weighing the evidence, and choosing from among conflicting factual inferences and conclusions those which he considers most reasonable, and *he has the inherent right to disregard the testimony of any witness* when he is satisfied that the witness is not telling the truth or her testimony is inherently improbable due to its inaccuracy, uncertainty, or interest or bias." (Emphasis added.) (Sun Life Assurance Co. of Canada v. Stacks, 7 Cir., 1951, 187 F. 2d 17, 20.)

And see, Acme Distributing Co. v. Collins, 9 Cir., 1957, 247 F. 2d 607, 611-612.

Appellate Courts should not disturb inferences drawn from facts:

"The District Court, having made findings substantially as stated above, proceeded to make additional findings of the existence of each of the facts on which an executive status, as defined by the Regulations, is made to depend. We believe that the evidentiary facts afford an adequate basis for the inferences drawn by the Court in making such additional findings. At the least, we think that *in drawing such inferences the Court was not clearly wrong, and conclude that the findings should therefore have been left undisturbed.* The Cir-

is more important, he may make his own inferences from the demeanor of the witnesses' which is

"always assumed to be in evidence."[28]

These facts are referred to because the taxpayers in their briefs use rather strong language in designating some twenty instances in which, they claim, the Tax Court has placed improper emphasis upon a particular fact. In reviewing these facts, this Court cannot scrutinize the record in order to find whether *one particular fact was properly evaluated or not.* Our function is to examine the record as a whole and determine whether the findings are sustained by substantial evidence, or whether, on the con-

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cuit Court of Appeals' rejection of those findings cannot rest on the conflicting testimony of petitioner's witnesses. The District Court heard the witnesses, and was the proper judge of their credibility." (Walling v. General Industries Co., 1947, 330 U.S. 545, 550.) (Emphasis added.)

[28]Wigmore on Evidence, 3rd Ed., 1940, Vol. III, § 946, p. 498. The late Judge Jerome Frank of the Court of Appeals for the Second Circuit has written what has become almost a classic comment on the significance of the demeanor of an orally-testifying witness as expressed in the brief statement quoted in the text from Wigmore:

"It is 'wordless language,' the liar's story may seem uncontradicted to one who merely reads it, yet it may be 'contradicted' in the trial court by his manner, his intonations, his grimaces, his gestures, and the like,—all matters which 'cold print does not preserve' and which constitute 'lost evidence' so far as an upper court is concerned. For such a court, it has been said, even if it were called a 'rehearing court,' is not a 'reseeing court'. Only were we to have 'talking movies' of trials could it be otherwise. A 'stenographic transcript correct in every detail fails to reproduce tones of voice and hesitations of speech that often make a sentence mean the reverse of what the words signify. The best and most accurate record is like a dehydrated peach; it has neither the substance nor the flavor of the fruit before it was dried'. It resembles a pressed flower. The witness' demeanor, not apparent in the record, may alone have 'impeached' him." Broadcast Music, Inc. v. Havana Madrid Restaurant Corp., 2 Cir., 1949, 175 F. 2d 77, 80.)

trary, there is clear error, or the Tax Court has applied an erroneous principle of law to conceded facts.

In dealing with the particular problem before us, there is *no one specific* test which the courts have evolved by which the question whether a sale is or is not in the usual course of trade or business can be determined. We have, heretofore, given many of the tests evolved in this and other courts.[29] In what precedes we have discussed their applicability to the facts in the instant case. What the Tax Court found in this case and what we think *they found correctly,* was that the taxpayers, engaged in "speculative building", over a period of years built residential properties under wartime restrictions while rentals and resale prices were limited. They resold them as soon as

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[29]The Court of Appeals for the Fifth Circuit has given an elaboration of these tests:

"What was the nature and character of the taxpayer's title to the property, the reason, purpose and intent of the acquisition and ownership and the period of its duration; and whether the property was held primarily for investment or as a part of the taxpayer's 'stock in trade', *i.e.*, as property bought, held and sold for profit?

"What was the vocation of the taxpayer at the time of the sales and prior thereto, whether a real estate broker or engaged in some similar or allied business, having in mind that they may have more than one business; and considering whether the taxpayer maintained only one office and that for his main vocation, and whether his engagement in the additional business was separable from his investment in the property?

"What was the extent of the taxpayer's activity and 'busyness' and whether the additional business was an occupational undertaking to which he habitually devoted time, attention or effort with substantial regularity; and, if the activities were conducted through a representative, whether those activities were carried on by the representative as a part of his own business and at his own expense or primarily in behalf of the taxpayer, and particularly the character and degree of supervision or control exercised by the taxpayer over the representative?" (Smith v. Dunn, 5 Cir., 1955, 224 F. 2d 353.)

prices rose and restrictions on resale of priority assisted housing were removed, making sales *nominally* through a broker, but, in reality, through their own organization, Associates, representing to buyers as an inducement, through advertising and by other means, "sale by builders" in which the broker's name nowhere appeared. Most of the paper work was in the name of the taxpayers, who executed escrow instructions and deeds in blank long in advance of a sale. For a short period of time, the funds were reinvested in stocks. But the taxpayers engaged again in speculative building activities, through new corporations in Colorado and Arizona within two years after completing these sales.

In sum, in arriving at the conclusion that these sales were made in the ordinary course of the taxpayers' business, the Tax Court found not one but, at least, four of the usual elements which courts deem determinative. These we summarize:

(a.) *The business of the taxpayers.* Both before and after this transaction the taxpayers were "speculative builders" of homes for profit which were disposed of as quickly as possible after they were built. In 1951, the New Mexico Corporation built 98 houses which were sold immediately. In 1952, the Colorado Corporation built 192 houses which were placed on the market for immediate sale. So that the sales here under consideration fitted into the pattern of their entire business activities.

(b) *Purpose of holding.* The Tax Court found an original rental object later changed into sale in the regular course of business. In the light of the preceding discussion, the Tax Court could have easily found that the rental episode was an incident forced upon the taxpayers by the fact that the resale price was controlled until October 15,

1945, when the price restrictions on resale were lifted, while rent control remained and that the intention to hold for sale existed at all times.[30]

(c) *Frequency and continuity of sales.* That the sales in the instant case meet the test of frequency and continuity cannot be questioned.

Sales activity on the 70 duplexes began early in 1946, and continued to July, 1946. Sales activity on the 100 duplexes began in August, 1946, and continued until about June, 1947. Sales went through escrow and were completed by months, as follows: In June, 1946, 19 sales; in July, 38 sales; in August, 10 sales; in September, 1 sale; in October, 25 sales; in November, 11 sales; in December, 17 sales; in January, 1947, 13 sales; in February, 18 sales; in March, 6 sales; in April, 2 sales; in May, 2 sales; in

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[30]Apposite here is the statement of this Court in Rollingwood Corp. v. Commissioner, 9 Cir., 1951, 190 F. 2d 263, 266:

"Although the requirements of the statute are to some extent overlapping, the emphasis in this case is whether the houses were held primarily for sale or primarily for rent. Petitioners contend that the word 'primarily' means 'principal' or 'chief', while the Commissioner contends it means 'essential' or 'substantial'. For reasons hereinafter stated we think the latter view is more consonant with the legislative policy.

"Suppose the taxpayer in the instant case intended to rent the houses for as long as he was required to do so under existing regulations and then to sell them. Or suppose his intention was to pursue whichever of these activities proved to be the most profitable, that is, if the *rental market* were good, he would continue to rent but if the *sales market* were high he would sell. In either of these suppositions we think it is fair to say that one of the essential purposes (in acquiring or holding the houses) is the purpose of sale. Under such circumstances, if the taxpayer does dispose of the houses by sale, is it within the legislative *purpose* to allow him to treat the proceeds of these sales as a capital gain? We think not." (Emphasis court's.)

June, 3 sales; in July, 3 sales. So it is evident that during most of 1946 and 1947, selling of the houses which their building company, Artcraft, had built was the only business of Associates, the taxpayers' partnership. The sales were continuous and substantial.

(d) *Activity of taxpayers in promoting sale.* Using the name of taxpayers' building corporation (Artcraft) as sellers, promoting sales, using taxpayers' office facilities and aid in financing, all are amply proved.[31]

The Supreme Court has warned us that the capital asset provision of our taxing statues

> "must not be so broadly applied as to defeat rather than further the purpose of Congress."[32]

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[31] See cases cited in Notes 5, 6 and 29.

[32] Corn Products Refining Co. v. Commissioner, 1955, 350 U.S. 46, 52. The Court elaborates:

> "Congress intended that profits and losses arising from the every-day operation of a business be considered as ordinary income or loss rather than capital gain or loss. The preferential treatment provided by § 117 applies to transactions in property which are not the normal source of business income. It was intended 'to relieve the taxpayer . . . from excessive tax burdens on gains resulting from a conversion of capital investments and to remove the deterrent effect of those burdens on such conversions'. Burnet v. Harmel, 287 U.S. at 106. Since this section is an exception from the normal tax requirements of the Internal Revenue Code, the definition of a capital asset must be narrowly applied and its exclusions interpreted broadly. This is necessary to effectuate the basic congressional purpose. *This Court has always construed narrowly the term 'capital assets'* in § 117." (Emphasis added.)

See, Simonsen Industries, Inc. v. Commissioner, 7 Cir., 1957, 243 F. 2d 407, 409.

So, if the facts are viewed in the light of this admonition and the criteria by which it is determined whether particular sales were carried on as a part of the taxpayers' busines , it becomes quite evident that the Tax Court was correct in denying the petitioners in this case the benefit of long-term capital gain and in holding that the sales were those of property held and sold for profit and disposed of in the ordinary course of the taxpayers' business.

The decisions of the Tax Court are affirmed.

(Endorsed:) Opinion. Filed Dec. 18, 1957.

Paul P. O'Brien, Clerk.

Office Supreme Court
APR 23 1958
JOHN T. FEY, Clerk

IN THE

# Supreme Court of the United States

October Term, 1957

No. 856

EDWARD POOL and LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY and EDNA MURPHY,

*Petitioners,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

## REPLY BRIEF FOR THE PETITIONERS.

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**On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.**

## REPLY BRIEF FOR THE PETITIONERS.

1. If the Tax Court's decision in this case had been reviewed by the Courts of Appeals for the Third, Seventh or Eighth Circuits, there would have been a reversal pursuant to the precedents established in those Circuits, and the taxpayers would have been held to have realized capital gain on the sale of property originally acquired for investment. The taxpayers have, however, been taxed in a different manner simply because their returns were filed in a geographic area within the jurisdiction of the Ninth Circuit and because that Court does not apply the same principles in cases of this kind.

The Commissioner, however, refuses to acknowledge the existence of a conflict, contending that nothing more

is involved than a factual question, that each case turns on its own record, and that, since no two cases are alike, differences in result at the appellate level "are not only inevitable but also appropriate." (Resp. Br. 16.)

But the hard fact is that the Circuits are applying diametrically opposed concepts to one of the most important and frequently litigated provisions of the Internal Revenue Code. And this would not be the first time that an important, frequently litigated issue was permitted to remain in a chaotic state for some time because the Government was, at first, so confused as to what are the factual elements of a case as to be unable to discern that decisional differences existed.[1] There are important differences here

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[1]A recent example will be found by comparing the Government's brief in opposition in *Stuyvesant Town Corp. v. United States*, 111 Fed. Supp. 243 (Ct. Cl.) certiorari denied, 346 U. S. 864 (No. 167, October Term, 1953) with its petition for a writ of certiorari in *United States v. Leslie Salt Co.*, 350 U. S. 383 (No. 793, October Term 1954).

In the former, the Government's brief in opposition was framed along the same lines as the one filed in this case, namely, that only a factual issue was involved, that the applicability of the statute depended on all the facts and circumstances, that neither the presence nor absence of any particular fact was controlling, and that each case turned on its own circumstances. The Government also, as it does here, pointed to the fact that it had refrained from applying for certiorari from earlier decisions adverse to it.

In the *Leslie Salt* petition (pp. 14-15), filed only one term later, and involving the identical issue, the Government contended that the differences between the Circuits "are differences as to the legal definition of 'debentures' and 'certificates of indebtedness' as those terms are used in the stamp tax statute", and admitted that it had been wrong in its earlier supposition that the varying decisions could "somehow be reconciled in terms of variations in the factual composites they represent."

We need scarcely add that this Court's decision in *Leslie Salt*, while adverse to the Government, did succeed in settling the basic principles involved and did result in the elimination of litigation in an area which had previously been the source of considerable controversy.

and they can and should be resolved by this Court to the end that future litigation will be minimized and that uniform results can be achieved by the lower courts.

The Commissioner's "why bother?" approach possesses a beguiling, initial simplicity. It would, indeed, be inappropriate for this Court to review an isolated fact question if the Courts of Appeals were applying similar standards and if differences in their decisions reflected nothing more than factual variations in the cases. But, the surface plausibility of this position is dispelled by even a cursory examination of what is involved, and a studied evaluation confirms that hard and fast differences exist between the Courts of Appeals.

The Solicitor General fails in his responsibility of assisting this Court in the selective process of certiorari when he substitutes pat phrases for the more painful process of reasoning and stamps "factual question" on a case where the contents will be found not to have been honestly labeled. And, surely avoidance of review by this Court and the possibility of a decision adverse to the Government should not be so important to warrant the gamble that a hasty reading of the Government's brief in opposition will not lay bare the coloring and occasional misstatement of facts, the use of misleading quotations from decisions, and its attempt to gloss over the conflict that does exist.

We cannot, we regret, be as terse as the Government's brief in opposition; but analysis and accuracy, while a lengthier process than misleading generalization, may eventually prove more helpful to an orderly, uniform development of the tax law.

2. We will avoid that "delusive simplicity" of attempting to draw unyielding lines between questions of law and

questions of fact, a goal which others have also found to be a "will-of-the wisp."[2]

Since a statute is involved, we submit that some generalizing principles have been established as the legislative standard, and that Congress did not intend that the lower Courts should have full freedom to arrive at willy-nilly results from case to case as though there were no ultimate guidelines and as though the decisional process involved nothing more than a throw of dice. We also submit that where the Courts of Appeals, while accepting the fact finder's version of the underlying facts, nevertheless reverse a lower court, they do so by the application of some standards derived from the statute and because of a conviction that the factual elements, as determined below, when fitted against the statutory standard, do not justify the ultimate conclusion reached.

Where some Courts of Appeals display a consistent pattern in the approach which they take under a particular section of the revenue law and that pattern is discernibly different from that followed by other Courts of Appeals, the net effect is one of a fundamental conflict of principle where litigants are taxed differently on transactions which are fundamentally the same. And, where the Courts of Appeals, in following such a pattern, consistently reverse the lower courts, the conflict is no less clear regardless of whether, in reversing, they frame their decisions

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[2]Isaacs, *The Law and the Facts*, 22 Col. L. Rev. 1. See also Paul, *Dobson v. Commissioner: The Strange Ways of Law and Fact*, 57 H. L. Rev. 753.

in terms of a clear mistake of law on the part of the lower court, or describe its conclusion as "clearly erroneous", or disagree with the criteria employed.

3. We turn, then, to examine the precise issue here to determine whether, as we maintain, there is a fundamental conflict between the Circuits or whether, as the Commissioner claims (Br. 16) these differences "are not only inevitable but also appropriate".

Specifically, the Tax Court has consistently taken the position that the purpose for which property is originally acquired is not of critical significance in determining whether subsequent sales are in the ordinary course of a trade or business so that, even if property was not originally acquired for resale in a business, later sales (if not made to a single purchaser) can constitute a trade or business, depending on the total factual complex, and that various criteria are to be employed in making that determination, including the frequency of the sales, how actively the sales were promoted, how actively the taxpayers were engaged in making the sales, what other business activities the taxpayers were generally engaged in, before, during, and afterwards, and what other business entities the taxpayers are interested in. The Tax Court's view of the statute is shared by the Court below, by other Courts of Appeals, and it also reflects the Commissioner's position.

If the Tax Court and these Courts of Appeals were correct in this premise, *i.e.*, that one can become engaged in a business when liquidating investment property by

piecemeal sales, and if all the Courts of Appeals were agreed on this principle, certiorari would not be appropriate.

But the fact is that the Third, Seventh and Eighth Circuits have rejected this basic premise. Those Courts demonstrably apply the principle that where property is originally acquired as an investment, the subsequent liquidation of the investment does not amount to the conduct of a business *regardless* of the frequency of the sales, the activity of the taxpayers in conducting the sales, their other business activity, etc., so that the criteria listed above are not, in the view of these Courts, relevant in these particular circumstances. If we are correct in this, the differences between the Courts of Appeals is not one which can be casually tossed aside as reflecting differences in judgment on factual variations.

It may be helpful, in demonstrating this, to compare the facts of this case with *Curtis Co. v. Commissioner*, 232 F. 2d 167 (C. A. 3rd) in accordance with the criteria which the Commissioner and the courts below deem significant.

| | Curtis Co. | Pool-Murphy |
|---|---|---|
| Nature of property | Houses | Houses |
| Purpose of original acquisition | Rental-investment; and not for sale to customers in ordinary course of business. Tax Court considered this not decisive. | Rental-investment; and not for sale to customers in ordinary course of business.[3] Tax Court considered this not decisive. |
| Purpose of liquidation | Market value had increased so that it was more profitable to sell than to continue to rent. | Market value had increased so that it was more profitable to sell than to continue to rent. |
| Frequency and continuity of sales | 1,386 houses sold to individual purchasers over a 4-year period. Tax Court found the sales were frequent and continuous. | 70 duplexes sold within 10-week period; 100 duplexes sold within 12-month period. |
| Activity of Taxpayer | Taxpayer a corporation. Sales made by ~~its own~~ employees who engaged in "aggressive sales effort." | Individual taxpayers. Sales made by broker. Taxpayers signed deeds and escrow instructions prepared by broker and helped obtain source of financing for some units. |
| Advertisements | Advertised by the taxpayer. | Advertisements composed, placed and paid for by broker. |

[3]See Petition, fn. 4, p. 11 and *infra*, p. 14.

| | CURTIS CO. | POOL-MURPHY |
|---|---|---|
| Other business activities | The corporate taxpayer, prior to, simultaneously with and immediately after the sales was engaged in an extensive business of building and selling other houses to customers. | Mr. Pool, fifteen years previously, had built houses for resale. Otherwise the taxpayers had not, individually nor as a partnership, bought and sold improved or unimproved real estate. Previously, all the taxpayers held the stock of a corporation, which had built and sold houses, and two of the taxpayers performed services for it. Four years after the sales, two of the taxpayers, together with a third person, owned the stock in and were employed by two corporations engaged in the business of building and selling houses. |
| Use of liquidation proceeds. | Apparently invested in the taxpayer's real estate business. | Invested in securities and in a rental building. |

The Commissioner asserts (Br. 17) that our assumed facts are not the record facts and that our reliance on *Curtis* "to show a conflict is thus misplaced". How do the facts which we state differ from those found by the Tax Court? The Commissioner chooses to be mute. And how do the facts of the present case differ from *Curtis?* The Commissioner does not say. If the differences are that: Curtis was simultaneously engaged in the business of building and selling houses for resale, while taxpayers were interested as officers and stockholders (in earlier and later years) in corporations so engaged and Pool had earlier been so engaged as an individual; that Curtis advertised and made the sales through its own employees, while the taxpayers here used a broker, signed the necessary papers and arranged some financing; that Curtis made a greater number of sales over a longer period of time (having more houses to sell), while the taxpayers sold less houses over a shorter period of time; that Curtis reinvested the proceeds in its real estate business, while the taxpayers invested in securities and in rental properties, we agree that there are differences. But they sharpen rather than dispel the existence of the conflict for they demonstrate that the Third Circuit would even more readily have reversed the Tax Court's decision in this case.

It would unduly extend our reply to make a similar, extended comparison with the facts of the other conflicting decisions of the Seventh and Eighth Circuits. We confidently state, however, that the Commissioner's criteria, whether considered singly or in totality, will not show any relevant distinctions between the cases. If the liquidation of an investment can be transformed into a business because the sales are frequent and extensive, are actively

promoted, because the taxpayers play some part in making the sales, and because the taxpayers have some contact, directly or indirectly, with some other recognized business of selling to customers, we submit that each of the other cases presented a stronger factual picture from the Government's point of view for the denial of capital gains.

The Commissioner does not quarrel with the correctness of these other decisions. And yet, surprisingly enough, he does not, because he obviously can not, point to one single factual element which would permit a rational distinction to be drawn or which would demonstrate why, if the Tax Court's decision here was properly affirmed, there was warrant for the reversals in these other cases.

The conclusion is inevitable that no valid distinguishing facts exist, and that the decisional results cannot be harmonized by some vague notion that a "fact" question is resolved.

4. The Courts of Appeals for the Third, Seventh and Eighth Circuit, contrary to the Commissioner, do recognize that a generalizing principle is involved, that their judgments have some more rational basis than is involved in a throw of dice, and that their views are in conflict with other Circuits.

For example, the Commissioner (Br. 18, fn. 13) says that in *Greenspon v. Commissioner*, 229 F. 2d 947, 952, the Eighth Circuit reached the conclusion "that the apparent conflicts are to be resolved by a 'more thorough and complete survey of the entire factual situation' ". What the Court actually said (p. 952) was that "perhaps *in some instances*" the apparent conflict can "be explained on the basis of factual differences" and it quickly added *"There*

*also appear to be differences in the law applied. It would be impossible to reconcile all the conflicting decisions . . .*" (Italics added). Significantly, it also observed that the cases denying capital gain treatment appear to do so by finding "a few similarities" with the way a business is ordinarily conducted and that "On the other hand, it would seem that in general the cases permitting capital gains treatment reached that result after *a more thorough and complete survey of the entire factual situation*". It was from this sentence that the Commissioner lifted the italicized language and transposed it to an opposite context.[4]

The Seventh Circuit, too, is of the view that it is applying a general principle in cases of this kind. Thus, in *Three States Lumber Co. v. Commissioner*, 158 F. 2d 61, 63, it said: "The conclusion of the Tax Court raises a clear-cut question of law . . ." And in *Chandler v. Commissioner*, 226 F. 2d 403, it held that it was reversible error for the lower court to conclude that very extensive, long-continued, piecemeal sales of tremendous acreage could be a business or taxed differently than if all the property had been sold at one time.

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[4]In attempting to establish that the Eighth Circuit regards the issue as one of pure fact, the Commissioner also makes it appear that the language quoted in his footnote 13, Br. p. 18, was from the Eighth Circuit's opinion in *Dillon v. Commissioner*, 213 F. 2d 218, 220, when it actually is from the Tenth Circuit's opinion in *Home Co. Inc. v. Commissioner*, 212 F. 2d 637, 641, and was set forth in *Dillon* with neither express approval nor disapproval. That in *Dillon*, as in *Greenspon*, the Eighth Circuit recognized that it was applying a general principle under the statute is evident from its rejection of the Tax Court's view that it was not significant that the taxpayer was liquidating an investment and its statement (p. 220) ". . . We think the principle applied is neither legal nor reasonable, but that it is clearly erroneous."

The Third Circuit is fully aware of the difference between a reversal of the Tax Court where the record does not support its view of the primary facts and a reversal based on its having applied the erroneous principle which is in issue here. In *Philber Equipment Corp. v. Commissioner*, 237 F. 2d 129, referring to the Tax Court's conclusion that the property was being held for sale to customers in the ordinary course of its trade or business, the Court of Appeals said (p. 131):

> "With respect to that finding it must be noted that it was in the nature of an ultimate finding of fact and since such finding is *but a legal inference* from other facts it is subject to review free of the restraining impact of the so-called 'clearly erroneous' rule applicable to ordinary findings of fact by the trial court, as we recently held in *Curtis Co. v. Commissioner*, 3 Cir. 1956, 232 F. 2d 167 . . ." (Italics added.)

To the extent that the Tax Court in *Philber* had found what was the original purpose in the acquisition of the property, the Court of Appeals recognized, pages 132-133, that it was reviewing a primary question of fact and overturned that finding because it was not supported by the record. To the extent that the Tax Court made an alternative conclusion, namely, that even if the property was not originally acquired for purposes of resale, the decisive factors were the intention to sell, the manner of sale, etc., the Court of Appeals recognized that an interpretation of the statute was involved and reversed because the Tax Court's reading of the statute was erroneous, saying (p. 133):

> "We cannot subscribe to this 'alternative ground'. To do so would make for judicial nullification of Section 117(j).

> "The essence of the Tax Court's alternative ground is that property changes character merely by the fact of its being exposed for sale. We agree with the taxpayer that such a concept is neither logical nor reasonable."

*Curtis Co. v. Commissioner*, 232 F. 2d 167, also proves the point. With respect to property (unimproved land) which the Tax Court had found, on conflicting evidence, to have been originally acquired for ultimate resale, the Court of Appeals recognized that the problem was essentially evidentiary and affirmed the holding that the proceeds were taxable as ordinary income, because (p. 171) "We cannot say under these circumstances that the Tax Court was wrong in reaching the conclusion which it did."

But, with respect to the houses which, concedely, were originally acquired for rental purposes, it reversed, even though the "criteria" which the Commissioner would apply were as strong or stronger as to the unimproved land as they were with respect to the houses. Thus, the difference in original purpose of acquisition was the crucial fact on which the appellate court reached different results as to different property in the very same case.

It was, undoubtedly, these considerations that convinced the court below (Pet. App. 4, fn. 6) that *Curtis* embodied a "seemingly contrary conclusion," even though the Commissioner is able to view all the decisions as being harmonious and appropriate in the different results which they embody.

5. We do not know, as we have previously observed, on what basis the Commissioner, in his attempt to negate the existence of a conflict, makes the assertion (Br. 17) that our "assumed facts" are not the record facts here.

We note that the Commissioner makes no attempt to document this false accusation. We also point out that, on the contrary, the Commissioner's summary (Br. 15) of the facts, which he says fully justify the decision below, is misleading and inaccurate. We shall enumerate:

(a) "Taxpayers acquired the property from Artcraft for rental or sale."

As to two of the taxpayers, Edward Pool and Lottie Pool, the express finding of the Tax Court was to the contrary, namely, that their purpose was to acquire and hold the properties for rental purposes. [R. 82-83.] As to William and Edna Murphy, the finding is less clear, but the Tax Court refrained from finding that there was an intent to sell to customers in a business. The Court of Appeals viewed the Tax Court as having found that *all* the taxpayers had (Pet. App. 31) "an original rental object later changed into sale . . ." See also Pet. 11, fn. 4.

Equally important is that the Tax Court did not believe that the original purpose was critical, for it taxed the Pools no differently than the Murphys, and it held here, as it has fairly uniformly, that the original purpose was not significant. This, of course, is the starting point for the division in the Circuits.

(b) "The houses were held only for rental during a period when war-time restrictions made sales less profitable than rentals." (Resp. Br. 15.)

There were no restrictions on the sales of these properties. There were restrictions on the selling price, *i.e.*, the price could not exceed $6,000 per unit, or fair market value, whichever was lower. [R. 39-40.] This restriction was removed by Executive Order on October 15, 1945. [R. 54.] Prior to the removal of this restriction, the fair

market price was *less* than the ceiling price and the same was true for some period thereafter [R. 362]. This is evident from the fact that of the first group of duplexes, sold in 1946, 64 were sold at *less* than ceiling price, at $5,900 per unit or $11,800 per duplex, and only 6 were sold at $6,100 per unit or $12,200 per duplex [R. 64].

It simply is not true, nor did the Tax Court make such a finding, that war-time restrictions made sales less profitable than rentals. It was the later return of servicemen which enhanced the value of real estate in this area and which made liquidation more profitable than a continued investment in rental housing subject to rent control.

(c) "As soon as the restrictions were removed, taxpayers terminated the leases and encouraged vacancies" (Resp. Br. 15).

The taxpayers did not terminate any leases. Sometime after April 10, 1946, the date when the last lease was written, the taxpayers adopted the policy of not renewing any expiring leases [R. 54]. This policy, moreover, was not adopted "as soon" as restrictions were removed on ceiling prices, but six months later. Vacancies were, quite obviously, not encouraged until there had been a decision to dispose of the properties and that was not until sometime in May, 1946, with respect to the 70 duplexes, and not until July or August, 1946, with respect to the 100 duplexes.[5]

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[5]In our petition (p. 20) we recognized that a taxpayer could impart values by personal efforts in improving, for purposes of resale, what was originally investment property and thus change the character of the property so that it would no longer qualify for capital gain. Compare the unreasoned statement by the Government (Resp. Br. 17, fn. 10) that failure to renew leases, permitting vacancies to occur, and selling a few houses to tenants "did change the rental property." And this is the only instance of where the Government offers a concrete argument as to how the factual elements fit the statute!

(d) "While a broker was hired to sell the houses, taxpayers advertised the houses for sale by the builders, and otherwise actively participated in the sales promotion, procuring the financing for many of the houses." (Resp. Br. 15.)

The Tax Court's finding is that the broker, not the taxpayers [R. 60] "wrote the copy for and placed and paid for the adversiting . . ." While some of the advertisements referred to Artcraft as the builder and some stated that the properties were being sold by the builder, the Tax Court did not find that these statements were known to the taxpayers and, indeed, it evidently attached no importance to the circumstance for it did not even mention it in its opinion.

The extent to which the taxpayers "actively participated in the sales promotion" amounted to no more than putting their signatures, sometimes in advance, on escrow instructions and on deeds which were prepared by the broker. Their signatures were, of course, a necessity for the passage of title. Murphy did assist in arranging for the financing of some of the properties.

(e) "After the sales of the housing units, taxpayers resumed the business of building and selling houses." (Resp. Br. 15.)

The Commissioner avoids mentioning that the proceeds of the sale were immediately invested in securities and in a rental building [R. 210-213, 514] and that it was not until 3 and 4 years later that Murphy and Pool, together with a third party, acquired the stock interest in and worked for two corporations engaged in building and selling houses (if that can accurately be described as a resumption of business by these two taxpayers).

The above is an analysis of the Commissioner's misleading summary of the relevant facts which he asserts (Br. 15) "warrants the Tax Court's conclusion". But even if this were an accurate summary, the pertinent question would still remain—how do the facts differ from *Curtis* (or the other cases on which we rely) and on what basis does the Commissioner concede that the Third Circuit's reversal in *Curtis* was correct, while the opposite conclusion is appropriate here?

We contend that no such basis can be found. The only possible conclusion is that, whether on the Commissioner's version of the facts or on the basis of the actual facts found by the Tax Court, the Third Circuit would have reversed the present decision on the authority of its *Curtis* and *Philber* decisions, as would the Seventh or Eighth Circuits, if this case had been reviewed there. There is, quite clearly, a serious conflict which ought to be resolved.

## Conclusion.

For the reasons stated in our Petition and amplified here, the Petition for a Writ of Certiorari should be granted.

Respectfully submitted.

IRVING I. AXELRAD,
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MITCHELL, SILBERBERG & KNUPP,
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April 21, 1958.

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No. 856

# In the Supreme Court of the United States

OCTOBER TERM, 1957

EDWARD POOL AND LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY AND EDNA MURPHY, PETITIONERS

*v.*

COMMISSIONER OF INTERNAL REVENUE

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT*

## BRIEF FOR THE RESPONDENT IN OPPOSITION

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# In the Supreme Court of the United States

OCTOBER TERM, 1957

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No. 856

EDWARD POOL AND LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY AND EDNA MURPHY, PETITIONERS

*v.*

COMMISSIONER OF INTERNAL REVENUE

---

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT*

---

## BRIEF FOR THE RESPONDENT IN OPPOSITION

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### OPINIONS BELOW

The memorandum findings of fact and opinion (R. 29–88) of the Tax Court are not officially reported. The opinion of the Court of Appeals (Pet. App. 1–34) is reported at 251 F. 2d 233.

### JURISDICTION

The judgment of the Court of Appeals was entered on December 18, 1957. (Pet. App. 34.) The petition for a writ of certiorari was filed March 15, 1958. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

### QUESTION PRESENTED

Whether, as the Tax Court and the Court of Appeals held, the income derived by taxpayers from the sales of certain real property was ordinary income under Section 22 of the Internal Revenue Code of 1939 and not capital gains from the liquidation of an investment under Section 117 (j).

### STATUTE AND REGULATION INVOLVED

Internal Revenue Code of 1939:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * *, or whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transfer of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> * * * * * *

(26 U. S. C. 1952 ed., Sec. 22.)

> SEC. 117. CAPITAL GAINS AND LOSSES.
>
> (a) *Definitions.*—As used in this chapter—
>
> (1) [as amended by Sec. 115 (b) of the Revenue Act of 1941, c. 412, 55 Stat. 687, and Sec. 151 (a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Capital assets.*—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or

business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (l) * * * or real property used in the trade or business of the taxpayer.

* * * * *

(j) [as added by Sec. 151 (b) of the Revenue Act of 1942, *supra*] *Gains and Losses From Involuntary Conversion and From the Sale or Exchange of Certain Property Used in the Trade or Business.*—

(1) *Definition of property used in the trade or business.*—For the purposes of this subsection, the term "property used in the trade or business" means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (l), held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not (A) property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year, or (B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business.

(2) *General rule.*—If, during the taxable year, the recognized gains upon sales or ex-

changes of property used in the trade or business, plus the recognized gains from the compulsory or involuntary conversion * * * of property used in the trade or business and capital assets held for more than 6 months into other property or money, exceed the recognized losses from such sales, exchanges, and conversions, such gains and losses shall be considered as gains and losses from sales or exchanges of capital assets held for more than 6 months. If such gains do not exceed such losses, such gains and losses shall not be considered as gains and losses from sales or exchanges of capital assets. * * *

* * * * *

(26 U. S. C. 1952 ed., Sec. 117.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

SEC. 29.117–1. *Meaning of Terms.*— * * *

The exclusion from the term "capital assets" of * * * real property used in the trade or business of a taxpayer is limited to such property used by the taxpayer in the trade or business at the time of the sale, exchange, or involuntary conversion. * * *

* * * * *

## STATEMENT

The facts as found by the Tax Court (R. 33–70), and adopted by the court below, may be summarized as follows:

The taxpayers, Edward Pool and Lottie Pool, and William K. and Edna Murphy, are husbands and wives. Arteraft Builders, Inc., is a California corporation organized March 10, 1941, and doing busi-

ness in Los Angeles, and later Long Beach. (R. 33–34.) At its inception, taxpayers were minority stockholders. Pool was president and Murphy sales manager. (R. 34–35.)

Taxpayer Pool had been a builder during all of his business life. Prior to 1935, when he moved to Long Beach, he had lived in Cincinnati, Ohio. During the period of his operations in the Cincinnati area and after moving to Long Beach, but prior to the organization of Arteraft, he had built houses both for sale on his own account and for others under contract. He had never built rental houses for his own account. Throughout his operations he sold all of his houses through brokers. He never had a real estate broker's license and never sold any houses personally (R. 35.)

Taxpayer Murphy moved to California from Illinois in 1933. Prior to that time he had been variously employed. For a short period he had done office work for a concern which built houses. About 1938, he started working as an employee of "Pacific Construction and Finance." While with that concern he worked on "rough drafts of sketches of apartment buildings and home layouts." This work continued until he became connected with Arteraft. He had never sold real estate or had a real estate broker's license. (R. 35.)

Arteraft was organized to engage in residential building construction. During 1941 most, if not all, of its business was that of constructing houses under contract for others. During 1942, the major portion of its income was derived from building houses for sale for its own account, although it did have some

income from building contracts. In 1942, it built for sale on its own account and sold 142 houses in Los Angeles County. In 1943, it built for sale on its own account and sold 188 houses, all of which were likewise located in Los Angeles County. It derived no income in 1943 from building under contract for others. (R. 34–35.)

On August 18, 1942, and February 17, 1943, Artcraft directors considered but turned down Pool's suggestion that it also build rental units. (R. 35–36.) Effective February 10, 1943, regulations imposing restrictions upon housing construction were issued, which entitled housing, approved by the Federal Housing Administration, to allocation of scarce building materials by the War Production Board. These regulations were known as General Orders Nos. 60–2 and 60–3 of the National Housing Agency.[1] Under No. 60–2, the housing was required to be held for rental, with an allowable option, in favor of the tenant only, to purchase at a maximum price of $6,000. (R. 39.) No. 60–3 implemented the restrictions by providing that any private housing, begun after February 10, 1943, was subject to the same rental and sale restrictions. (R. 40.)

On February 23, 1943, Artcraft filed its first application, to build an apartment house,[2] and on May 26,

---

[1] The substance of the orders is set forth in the findings of fact (R. 38–41), and opinion below (Pet. App. 11–13). See 8 Fed. Register 1829–1831.

[2] The date of this application is of some significance here, but gains from the sale of this apartment house are not involved in this case.

1953, another application to build 70 duplexes on Tract 11451. Both of these applications were approved in June 1943. (R. 38.)

In April 1943, by the issuance to them of additional shares of stock, taxpayers became majority stockholders of Artcraft, and on or about June 1, 1943, by purchase of the minority shares, they became the sole stockholders and officers and directors of Artcraft. It was the testimony of Pool and Murphy that the minority stockholders did not desire to engage in construction of rental housing. (R. 37.)

On September 16, 1943, at a special meeting of Artcraft's directors, an agreement was entered into for the sale of these tracts, on which the approved housing was to be built, to the four individual taxpayers as tenants in common. The agreement, expressed in a motion of the directors, stipulated that the taxpayers were to pay all existing and future mortgages or other obligations against the properties out of the moneys received from "the sale, hypothecation or rentals of said properties". It was further stipulated that the taxpayers were to have no personal liability for payment of mortgages or other obligations against the properties other than from the moneys received from "sales, hypothecation or rentals of said property." (R. 41–42.) It was further stipulated that all profits "from the sale, rental or hypothecation of the properties" over and above said indebtedness should be the sole exclusive property of the four taxpayers as tenants in common. (R. 43.)

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The units were rented, as construction was completed, on one-year written leases. On March 13, 1944, all of the units being completed, the agreement to sell the properties to taxpayers was consummated in accordance with its terms, the taxpayers agreeing that they would pay all incumbrances against said properties "so long as rentals or sales of said properties produced sufficient funds" therefor. (R. 44–45.)

On or about April 1, 1944, taxpayers formed a joint venture (or partnership) known as Edward Pool and Associates (referred to as Associates) for the purpose of holding and dealing with the properties which had been transferred to them by Arteraft. (R. 46–47.)

On January 4, 1945, Arteraft made a third application for the construction of 109 duplexes on Tract No. 13163, Long Beach, subject to the requirements of General Orders Nos. 60–2 and 60–3. The application was approved on February 5, 1945, and on February 26, Arteraft agreed to transfer this property and the buildings to be constructed thereon to taxpayers, upon the same terms and conditions with respect to payment of encumbrances against the property out of rentals or sales as was previously agreed to. (R. 48–49.) It was likewise further stipulated that all profits remaining from the rental, sale, or hypothecation, over and above the amount of the mortgage indebtedness, would be the sole and exclusive profit of the four individual taxpayers. (R. 50.)

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[1] It is the gains from the sale of the 109 duplexes on this Tract No. 13163 and the 70 duplexes on Tract No. 11451 that are involved in this case.

On February 1, 1946, this set of duplex housing units having been fully completed, the agreement for the transfer of the properties to the taxpayers was carried out in accordance with its terms. (R. 50–52.) The 100 duplexes on this last tract, Tract No. 13163, were rented on one-year written leases. None of the leases of the 170 units included a purchase option provision, and tenants were advised that the houses were not for sale. (R. 54.)

Effective October 15, 1945, the sales ceilings were removed, but rent controls remained in force. An application by taxpayers and Arteraft for permission to increase rents was denied, and, thereafter, the one-year leases were not renewed when they expired, but the tenants were continued on a month-to-month tenure. The date of the last written lease was April 10, 1946. (R. 54.)

During this period, the Associates maintained no office and had no employees. Its books were kept by an employee of Arteraft. Moreover, the properties were managed by Arteraft which signed the leases as lessor, collected the rents and made the payments, less its commission and expenses, to Associates. (R. 55.)

In October 1945, after the controls on sales prices of war housing had been lifted, there was a very substantial rise in the market price for the type of housing owned by taxpayers. Some time in January or February of 1946, one Philip Boland, a real estate broker, suggested to Pool and Murphy that they permit him to sell the duplexes for them. The proposal was first accepted by Murphy, but Pool did not

agree to it until some time later. An agreement was reached with Boland for the sale of the 70 duplex units on Tract No. 11451 for a flat $500 per unit commission, the taxpayers to supply the office facilities and secretarial help. (R. 57–58). Boland advised Murphy that the gains realized upon the sale of the properties would be capital gains, and Murphy received the same advice from his accountant. (R. 58–59.)

The sale activities on the 70 duplexes on Tract 11451 began in May 1946, and continued to July 1946. The properties were advertised as having been built by Artcraft and for sale by the builder. All of the 70 duplexes were sold in ten weeks' time, the last sale being made on September 6, 1946. (R. 60.)

Meantime, in July 1946, taxpayers and Boland reached a similar agreement for the sale of the 100 duplexes on Tract 13163. The selling operation was conducted in the same manner as the first set, except that Boland, for part of the time at least, employed two salesmen to assist him. The arrangements for financing the sale of the 100 duplexes were made by taxpayer Murphy with an insurance company. The duplexes were advertised as having been built by Artcraft and for sale by the builder. R. 60–62.)[4] The 100 duplexes were sold in the period from August 1946 to June 1947, the longer period being due in part to rent control, which prevented taxpayers from having the properties vacated preparatory to sale.

[4] The text of a typical advertisement is set forth in the opinion below. (Pet. App. 23.)

The creation of vacancies was encouraged, and comparatively few of the units were sold to the tenants. (R. 61–62.)

The 70 duplexes were sold for a total of $828,400 and the 100 duplexes were sold for a total of $1,289,000. (R. 64–65.)

In 1950, taxpayers Pool and Murphy, with a third person, formed a corporation in New Mexico, with Pool as president and Murphy as secretary-treasurer, which engaged in the business of building and selling 98 single-family dwellings. In 1951, the same three individuals formed a corporation in Colorado, with the same officers, which engaged in the same business, selling 192 homes. (R. 67.)

On these facts, after first disposing of certain issues not in controversy here,[5] the Tax Court found that, beginning with the employment of Boland, the four taxpayers began a business of selling real estate, and from April 1946, the 70 duplexes on Tract 11451, and from July 1946, the 100 duplexes on Tract 13163, were held by them primarily for sale to customers in the ordinary course of that business. (R. 70.) Accordingly, the Tax Court held that the gains from the sale of the 170 duplexes were gains from the sale of property used in the trade or business of taxpayer within the meaning of Section 117 (j), and hence were not capital gains on the sale of capital assets within the meaning of Section 117 (a).

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[5] These issues related to the question of the taxation of the transfer of the properties from Arteraft to taxpayers. (R. 70–80.)

The Tax Court noted that no rigid rule can be formulated to determine the issue and that in the end each case must stand upon its own peculiar facts and circumstances. (R. 82.) It reviewed the evidence (R. 82–88), pointing out that, at the time of the distribution of the properties by Arcraft to taxpayers, their purpose was mixed, and that there was no question that, after the distribution and before being placed on the market, the properties were used in the conduct of a rental business. (R. 82–83.) However, the Tax Court concluded that taxpayers were not liquidating an unprofitable rental business, but entering a more profitable sales business. (R. 86.) As the Tax Court said (R. 87): "All of the facts considered, it would be difficult to imagine a selling operation or business which was more actively conducted and carried on than the one here."

The Court of Appeals, as its opinion shows, also carefully reviewed the evidence. (Pet. App. 14–34.) On the basis of all the facts, the court sustained the findings of the Tax Court. In its view of the evidence, taxpayers' main business was selling; they acquired the properties in question for rental or sales; they were forced into rental as an incidental business by the wartime restrictions on the sale of housing; and they returned to their sales business as soon as price restrictions were lifted. (Pet. App. 30–31.) In any case, the court below held, even if the properties were originally held for rental, the Tax Court's finding that taxpayers changed their original rental objective into sale in the regular course of business

was amply supported by the undisputed facts of taxpayers' business, purpose of holding, frequency and continuity of sales, and the activity of the taxpayers in promoting sales. (Pet. App. 31–33.)

## ARGUMENT

The question presented is one of fact, and the court below correctly affirmed the Tax Court's determination. There is no conflict and no occasion for further review.

1. Section 117 (j) of the Internal Revenue Code of 1939 (*supra*, pp. 3–4) accords preferential capital gain treatment to gains from sales of depreciable business property held for more than six months, but expressly excepts from its coverage property "held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business"[6] Whether particular property falls within the excepted category presents a question of ultimate fact in each case, no one factor being decisive, and the trial court's conclusion should not be disturbed unless clearly erroneous. Among the relevant factors to be considered and weighed are the business of the taxpayer, intention or purpose of the taxpayer in acquiring and holding the property, frequency and continuity of sales, the methods used in making the sales such as advertising or other sales promotion, and any other circumstances bearing upon whether the sales are in furtherance of the taxpayer's

[6] No change in the law, so far as the sale of housing properties is concerned, was made by the corresponding sections of the 1954 Code. Compare Section 117 (a) of the 1939 Code with Sec. 1221 of the 1954 Code, and Sec. 117 (j) with Section 1231 (b) (1). It is to be noted that a specific test for distin-

business.[7] This Court has declined to review similar cases which presented like questions of a factual nature.[8] Because of the inappropriateness of Supreme Court review in cases of this kind, the Government has refrained from seeking certiorari where the de-

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guishing between sale of capital assets and ordinary business was established in the 1954 Code *only* for the sale of vacant land subdivided into lots (Section 1237).

[7] Cases in the courts of appeals involving the question here presented are legion, and they hold that the question is one of fact. See, *e. g.*, *Monday* v. *Commission* (C. A. 6th), decided February 20, 1958 (58–1 U. S. T. C., par. 9323); *Philber Equipment Corp.* v. *Commissioner*, 237 F. 2d 129 (C. A. 3d); *Harry Slatkin Builders* v. *Commissioner*, 235 F. 2d 189 (C. A. 6th), certiorari denied, 352 U. S. 928; *Curtis Co.* v. *Commissioner*, 232 F. 2d 167 (C. A. 3d); *Pacific Homes* v. *United States*, 230 F. 2d 755 (C. A. 9th); *Homann* v. *Commissioner*, 230 F. 2d 671 (C. A. 9th); *Greenspon* v. *Commissioner*, 229 F. 2d 947 (C. A. 8th); *Chandler* v. *United States*, 226 F. 2d 403 (C. A. 7th); *Cohn* v. *Commissioner*, 226 F. 2d 22 (C. A. 9th); *Smith* v. *Dunn*, 224 F. 2d 353 (C. A. 5th); *Goldberg* v. *Commissioner*, 223 F. 2d 709 (C. A. 5th); *Shearer* v. *Smyth*, 221 F. 2d 478 (C. A. 9th), certiorari denied, 350 U. S. 840; *Galena Oaks Corp.* v. *Scofield*, 218 F. 2d 217 (C. A. 5th); *Dougherty* v. *Commissioner*, 216 F. 2d 110 (C. A. 6th); *Dillon* v. *Commissioner*, 213 F. 2d 218 (C. A. 8th); *Home Co.* v. *Commissioner*, 212 F. 2d 637 (C. A. 10th); *Victory Housing No. 2* v. *Commissioner*, 205 F. 2d 371 (C. A. 10th); *Palos Verdes Corp.* v. *United States*, 201 F. 2d 256 (C. A. 9th); *Winnick* v. *Commissioner*, 199 F. 2d 374 (C. A. 6th); *Mauldin* v. *Commissioner*, 195 F. 2d 714 (C. A. 10th); *Rollingwood Corp.* v. *Commissioner*, 190 F. 2d 263 (C. A. 9th); *King* v. *Commissioner*, 189 F. 2d 122 (C. A. 5th), certiorari denied, 342 U. S. 829; *Rubino* v. *Commissioner*, 186 F. 2d 304 (C. A. 9th), certiorari denied, 342 U. S. 814; *Three States Lumber Co.* v. *Commissioner*, 158 F. 2d 61 (C. A. 7th).

[8] See, *e. g.*, *Harry Slatkin Builders* v. *Commissioner*, *supra*; *Shearer* v. *Smyth*, *supra*; *Rubino* v. *Commissioner*, *supra*; *King* v. *Commissioner*, *supra*.

cision has been adverse to it.[*] There is no more occasion for further review of this case than of others involving comparable questions.

2. The record amply warrants the Tax Court's conclusion that the property here involved—duplex housing units—was held by taxpayers in their business primarily for sale to customers. Taxpayers' business before the sales in question was that of building and selling houses, which were built by taxpayers' wholly-owned building and sales corporation, Artcraft. Taxpayers acquired the property from Artcraft for rental or sale; the houses were held only for rental during a period when wartime restrictions made sales less profitable than rentals; the rentals were managed for taxpayers by their corporation, Artcraft; and, as soon as the restrictions were removed, taxpayers terminated the leases and encouraged vacancies. While a broker was hired to sell the houses, taxpayers advertised the houses for sale by the builders, and otherwise actively participated in the sales promotion, procuring the financing for many of the houses. The sales were frequent and conducted over a two-year period, and after the sales of the housing units, taxpayers resumed the business of building and selling houses.

On the basis of these facts, the Tax Court was fully justified in concluding that the properties were held primarily for sale to customers in the ordinary course of their business. (R. 70.) Under familiar rules

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[*] See, *e. g.*, *Philber Equipment Corp.* v. *Commissioner*, *supra*; *Smith* v. *Dunn*, *supra*; *Goldberg* v. *Commissioner*, *supra*; *Curtis Co.* v. *Commissioner*, *supra*.

governing the scope of judicial review of the trial court's factual determination, the court below was equally justified in sustaining its decision. Both courts below having decided the factual issue against taxpayer, their concurrent findings are entitled to finality here. *Corn Products Co.* v. *Commissioner*, 350 U. S. 46, 51.

3. There is no conflict. Since the question is factual, each case in this field turns, as it must, on its own record. In view of the wide variations in evidentiary content of such cases, differences of result are not only inevitable but also appropriate. That an appellate court may have been warranted in reversing a trial court's decision in some other case involving a similar question scarcely furnishes a basis for assuming, as do the taxpayers, that the court below was obliged to reverse in this case.

Taxpayers' entire argument rests upon their assertion that, having originally held the property for investment, they decided to liquidate and accordingly sold the property in its existing condition piece-by-piece, as expeditiously as possible and at the best possible prices, employing a broker to conduct the sale. (Pet. 8, 20.) On these assumed facts of the case, taxpayers contend that the decision below is in direct conflict with the decisions of the Third, Seventh, and Eighth Circuits, and especially the decision of the Third Circuit in *Curtis Co.* v. *Commissioner*, 232 F. 2d 167 (Pet. 9–14, 20); and that the decision below applies an erroneous rule of law that the gains from the sale of investment property in the same manner

as the active conduct of a business can be taxed as ordinary income. (Pet. 14, 20.)

The entire argument falls, however, because the assumed facts are not the facts found by the Tax Court, sustained by the court below, and conclusive here.[10] Taxpayers' heavy reliance upon *Curtis Co.* v. *Commissioner* to show a conflict is thus misplaced.[11] Indeed, the *Curtis* decision expressly approved the rule of law which the courts below applied here—namely, that preferred capital-gain treatment on sales of investment property is precluded if "the purpose of the sales is primarily making money by carrying on a substantial part of the activities of a person engaged in the business of selling houses."

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[10] See *supra*, pp. 4–11, 15. This is further shown by taxpayers' attack on the factual findings, *e. g.*, their assertion that the court below "attributed erroneously" the selling activities of the real estate broker to taxpayer. (Pet. 20.) In this connection, it may be noted that the Tax Court and the court below went on to find that, independently of the broker's activities, "There are other facts that show active participation by the taxpayers in the conduct of the sales." (Pet. App. 25–27, R. 61–62, 87.) Moreover, taxpayers concede, as they must, that a taxpayer can change from an investment business to the ordinary sales business if he improves or changes the property before sale. (Pet. 20–21.) Taxpayers here did change the rental property to make it saleable; *i. e.*, they terminated all written one-year leases and encouraged vacancies, and few houses were sold to tenants. (R. 54, 62.)

[11] Compare the summary statement of the facts of the *Curtis* case (232 F. 2d 169) with the summary by the court below. (Pet. App. 30–33.) The facts of *Philber Equipment Corp.* v. *Commissioner*, 237 F. 2d 129 (C. A. 3d), are clearly different from those at bar.

(232 F. 2d 169).[12] And, as the *Curtis* opinion states, the decision in each case turns upon the facts, which are "as variable as human activities." (232 F. 2d 170.) The other decisions relied upon by taxpayers for a showing of conflict (Pet. 13–14) are to the same effect.[13]

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[12] Again at page 170, the *Curtis* opinion states the question to be "whether on these facts the conclusion is supportable that petitioner went *ad hoc* into the ordinary course of business when it sold these rental properties."

[13] Thus, in *Greenspon* v. *Commissioner*, 229 F. 2d 947, 951–952, the Eighth Circuit, reviewing the decisions and after first noting an apparent conflict of law, reached the conclusion that the apparent conflicts are to be resolved by "a more thorough and complete survey of the entire factual situation."

In *Dillon* v. *Commissioner*, 213 F. 2d 218, 220, the Eighth Circuit stated the very rule which taxpayers contend is erroneous:

> One may, of course, liquidate a capital asset. To do so it is necessary to sell. The sale may be conducted in the most advantageous manner to the seller and he will not lose the benefits of the capital gain provision of the statute, unless he enters the real estate business and carries on the sale in the manner in which such a business is ordinarily conducted. In that event, the liquidation constitutes a business and a sale in the ordinary course of such a business and the preferred tax status is lost.

It is to be noted that the *Dillon* court derived this rule from *Home Co.* v. *Commissioner*, 212 F. 2d 637 (C. A. 10th), where the court reached the opposite factual conclusion that the sales were in the ordinary course of business.

## CONCLUSION

For the reasons stated, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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APRIL 1958.

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IN THE

# Supreme Court of the United States

October Term, 1957

No. 856

EDWARD POOL and LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY and EDNA MURPHY,

*Petitioners,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

## PETITION FOR REHEARING.

IRVING I. ANGERAD,
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*Attorney for Petitioners.*

IN THE

# Supreme Court of the United States

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EDWARD POOL and LOTTIE POOL, EDWARD POOL, LOTTIE POOL, WILLIAM K. MURPHY, EDNA MURPHY, WILLIAM K. MURPHY and EDNA MURPHY,

*Petitioners,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE.

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.**

## PETITION FOR REHEARING.

*To the Honorable, the Chief Justice, and the Associate Justices of the Supreme Court of the United States:*

Come now the Petitioners in the above entitled case, by their attorney, Irving I. Axelrad, and respectfully petition this Court for reconsideration of the Order entered April 28, 1958, denying the Petition for a Writ of Certiorari in this case.

1. As grounds for this Petition for Rehearing, Petitioners invite attention to the decision of the Sixth Circuit in *Yunker v. Commissioner*, decided on May 1, 1958 (not yet officially reported, but reproduced at paragraph

9487, C. C. H. Standard Federal Tax Reports), where the Tax Court was again reversed for having interpreted the statute in the same way as it did in the present case.

The *Yunker* case, decided subsequent to the denial of certiorari in this case, is opposed, in principle, with the decision of the Court of Appeals below. The *Yunker* decision demonstrates that, contrary to the decision of the Court below and the position of the Solicitor General, the Sixth Circuit, like the Third, Seventh and Eighth Circuits, agrees that, where there is no dispute concerning the underlying facts, the question posed in a case like this is one where "the reviewing court is not bound by the findings of ultimate fact below" and that what is involved is "the interpretation of the statute" where the phrases " 'trade or business,' 'ordinary' and 'customers' are to be construed in their ordinary and not in an artificially created meaning."

The *Yunker* decision also demonstrates that the Sixth Circuit, contrary to the decision of the Court below and the position of the Solicitor General, agrees with the Third, Seventh and Eighth Circuits that where property is not originally acquired for resale (acquired by inheritance in *Yunker*), the facts that it is disposed of by piecemeal sales, that there are sales promotions and advertising, and that the sales are frequent and continuous, do not justify the Tax Court's ultimate conclusion that the sales are made in the course of a business.

In fine, the Sixth Circuit, contrary to the decision of the Court below and the position of the Solicitor General, agrees with the Third, Seventh and Eighth Circuits that, where property is originally acquired for purposes other than resale, an ultimate disposition by numerous sales is

not to be taxed differently than would have been the case if all the property had been sold at one time; the opinion states:

> "If petitioner had sold the entire tract at a profit, in one transaction, it is unquestioned that she would be entitled to capital gains treatment. It was impossible for her to sell the entire tract at one time at a profit. To hold that she would not be entitled to capital gains treatment, when she would otherwise be entitled to it, merely because she selected the only possible method of selling her property at a profit, by installing improvements and selling in smaller parcels, would seem to be an injustice resulting from a forced and artificial construction of the statute, which, in our view, could not have been intended by Congress."

It should be emphasized that in *Yunker* the sales were taxed as capital gains even though the property was improved in order to make it more salable while in the present case, the property was sold "as is."

And, in contrast to the position of the Solicitor General to the effect that there is no dissension among the courts, the Sixth Circuit recognized in the *Yunker* opinion that "some courts differ in their conclusions in resolving the problem posed in this case . . . ." Thus, the Sixth Circuit, like the Eighth and Ninth Circuits, has taken cognizance of the existing divergent judicial views concerning the meaning of the statute. See our Reply Brief, pages 10-13.

2. As a further ground for this Petition for Rehearing, Petitioners show that on April 24, 1958, a Reply was filed to the Commissioner's Brief in Opposition in this,

case, pointing out serious errors in the Commissioner's contentions that there are no conflicting decisions. These errors consist of serious misstatement of the facts of the subject case, of the holdings of the cases which we asserted to be in conflict with the decision below, and distorted reproduction of language from opinions of other Courts of Appeals. Even after the fullest allowance for the zeal of advocacy, we believe the Commissioner's brief in opposition so far oversteps an acceptable norm that it may well have misled this Court. This is particularly so because of the reliance which this Court must inevitably place on the Solicitor General's views in the selective process of certiorari.

Petitioners' reply brief, filed as promptly as airmail service between Washington and Los Angeles and printing and writing would permit, was filed with the Court on April 24, 1958, just one week after the brief in opposition was filed. This may have been too late for effective consideration by the Court in acting on the petition.

The additional grounds, therefore, upon which Petitioners seek a rehearing and on which they urge that certiorari be granted are those fully stated in the reply brief because those grounds may not have been available to the Court prior to acting on the petition. Accordingly, to avoid repetition, we respectfully refer this Court to the reply brief for a full statement of those grounds and a clear demonstration that there is a direct and serious conflict on the meaning of the statute which was erroneously applied by the Court below.

## Conclusion.

This Petition for Rehearing should be granted, the Order denying certiorari should be withdrawn, and the Petition for Writ of Certiorari should be granted.

Respectfully submitted,

IRVING I. AXELRAD,
*Attorney for Petitioners.*

MITCHELL, SILBERBERG & KNUPP,
*Of Counsel.*

May 20, 1958.

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## Certificate of Counsel.

Irving I. Axelrad, counsel for the Petitioners in this case, does hereby certify that the annexed Petition for Rehearing is presented in good faith, and not for delay, and that substantial grounds exist for a rehearing which were not presented to and, in part, may not have been available to the Court prior to its having reached its decision to deny the Petition for a Writ of Certiorari.

IRVING I. AXELRAD.